No. 2254

United States
Circuit Court of Appeals
For the Ninth Circuit.

R. H. HERRON COMPANY, a Corporation,

Appellant,

vs.

WILLIAM H. MOORE, Jr., Trustee in Bankruptcy of the CLEVELAND OIL COMPANY, a Corporation,

Appellee.

Supplemental Transcript of Record.

Upon Appeal from the United States District Court for the Southern District of California, Southern Division.

FILMER BROS. CO. PRINT, 330 JACKSON ST., S. F., CAL.

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INDEX OF PRINTED TRANSCRIPT OF RECORD.

[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur. Title heads inserted by the Clerk are enclosed within brackets.]

[Proof of Debt Due R. H. Herron Co.]

In the District Court of the United States for the Southern District of California, Southern Division.

IN BANKRUPTCY.

In the Matter of CLEVELAND OIL COMPANY, Bankrupt.

At Los Angeles, in said Southern District of California, on the 22 day of May, 1911, came John M. Sands, of the city of Los Angeles, in the county of Los Angeles, State of California, and made oath and says:

That he is the Vice-president and Treasurer of the R. H. Herron Company, a corporation, incorporated under the laws of the State of California, and carrying on business, and having its office and principal place of business at said city of Los Angeles, county of Los Angeles, State of California, in said Southern District; and that he is duly authorized to make this proof of debt on behalf of said R. H. Herron Company, and says that the said Cleveland Oil Company, the person against whom a petition for adjudication of bankruptcy has been filed, was at and before the filing of said petition, and still is, justly and truly indebted to said R. H. Herron Company, a corporation, in the sum of Fourteen Thousand, Eight Hundred Four and 32/100 ($14,804.32) Dollars;

That the consideration of said debt is as follows: Fourteen Thousand Four Hundred Seventeen and

36/100 ($14,417.36) Dollars, being and representing the principal of a balance due to the said R. H. Herron Company by the said bankrupt on account of goods, wares and merchandise sold and delivered by the said R. H. Herron Company to the said bankrupt at its special instance and request, and the sum of Three Hundred Eighty-six [2*] and 96/100 ($386.96) Dollars, being interest charges due and owing upon said principal sum of Fourteen Thousand Four Hundred Seventeen and 36/100 ($14,417.36) Dollars according to agreement had between the said R. H. Herron Company and the said bankrupt; an itemized account of which showing the various debits and credits is filed herewith, marked Exhibit "A" and expressly made a part of this proof of debt.

That all of the said sum of Fourteen Thousand Eight Hundred Four and 32/100 ($14,804.32) Dollars is past due and payable.

That included in the above principal sum of Fourteen Thousand Four Hundred Seventeen and 36/100 ($14,417.36) Dollars are four promissory notes, true and correct copies of which are filed herewith, marked Exhibit "B" and expressly made a part of this proof of debt.

That the total amount of said promissory notes which were given by said bankrupt to the said R. H. Herron Company on account of said debt of Fourteen Thousand Eight Hundred Four and 32/100 ($14,804.32) Dollars is the sum of Twelve Thousand Seven Hundred Twenty-six and 68/100 ($12,726.68) Dollars, on which has been paid by said bankrupt the

*Page-number appearing at foot of page of original certified Record.

sum of Four Thousand Six Hundred Eighty-five and 85/100 ($4,685.85) Dollars, leaving a balance due as principal on said promissory notes of the sum of Eight Thousand Forty and 83/100 ($8,040.83) Dollars.

That no part of said debt of Fourteen Thousand Eight Hundred Four and 32/100 ($14,804.32) Dollars has been paid; that there are no off sets or counterclaims to same, and that said corporation has not, nor has any person by its order or to the knowledge or belief of said deponent for its use, received any manner of security for said debt from said bankrupt, except Ten (10) Bonds of said bankrupt, numbering from #57 to 66, inclusive, for Five Hundred (500.00) Dollars each, total Five Thousand [3] (5000.00) Dollars, and having possible value of ten (10) cents on the dollar.

That no judgment has been obtained or entered in favor of said R. H. Herron Company and against said bankrupt for said sum of Fourteen Thousand Eight Hundred Four and 32/100 ($14,804.32) Dollars, or any portion thereof, nor have any notes been taken for the same, except as hereinbefore specified and set forth.

JOHN M. SANDS,

Treasurer of said R. H. Herron Company, a Corporation.

Subscribed and sworn to before me this 22 day of May, 1911.

[Seal] RALPH BANDINI,

Notary Public, in and for the County of Los Angeles, State of California.

[Endorsed]: No. ———. In the District Court of the United States for the Southern District of California, Southern Division. In the Matter of Cleveland Oil Company, Bankrupt. Proof of Debt. Filed May 22, 1911, at —— o'clock —— M. Lynn Helm, Referee. $14,804.32. Geo. E. Whitaker, Stoner Block, Bakersfield, Cal., Attorney for Creditor. [4]

In the United States District Court, Southern District of California, Southern Division.

IN BANKRUPTCY—No. 686.

In the Matter of the CLEVELAND OIL COMPANY,

A Bankrupt.

Objections to Claim of R. H. Herron Company.

William H. Moore, Jr., the duly appointed, qualified and acting trustee of the Estate of the Cleveland Oil Company, a bankrupt, objects to the allowance of the claim of R. H. Herron Company heretofore filed herein, on the following grounds, to wit:

I.

That a petition for the adjudication of said Cleveland Oil Company, a corporation, a bankrupt, was filed in the above-entitled court on the twelfth day of January, 1911.

II.

That within four months preceding the filing of said bankruptcy petition herein, to wit, on the fifteenth day of September, 1910, the said bankrupt, while insolvent, transferred to said R. H. Herron

Company, who was then, and still is, a creditor of said bankrupt, the sum of Two Thousand Dollars, ($2,000.00) in cash, and said transfer was made to apply upon a pre-existing debt owed by the bankrupt to said creditor, and the effect of said transfer is to give said creditor a greater percentage of its claim than the other creditors of the same class.

III.

That on or about the thirty-first day of October, [5] 1911, and within four months preceding the filing of said bankruptcy petition herein, said bankrupt, while insolvent, transferred to said R. H. Herron Company, who was then, and still is, a creditor of said bankrupt, certain oil well casing, of the value of Two Thousand Eight Hundred Twenty-three Dollars, Thirty-seven Cents ($2,823.37), and said transfer was made to apply upon a pre-existing debt owed by the bankrupt to said creditor, and the effect of said transfer is to give said creditor a greater percentage of its claim than other creditors of the same class.

IV.

That within four months preceding the filing of said bankruptcy petition herein, to wit, on or about the thirty-first day of December, 1910, the said bankrupt, while insolvent, transferred to said R. H. Herron Company, who was then, and still is, a creditor of said bankrupt, two pumps, of the reasonable value of Three Hundred Dollars ($300.00), and said transfer was made to apply upon a pre-existing debt owed by the bankrupt to said creditor, and the effect of said transfer is to give said creditor a greater per-

centage of its claim than other creditors of the same class.

V.

Said R. H. Herron Company, the said creditor, received said cash and said property with a reasonable cause for believing that a preference was intended to be given it thereby, and said R. H. Herron Company has not surrendered said property so received by it as aforesaid.

WHEREFORE, your trustee prays that the said claim of said R. H. Herron Company be not allowed, unless said preferences be surrendered.

WM. H. MOORE, Jr.,
Trustee of the Estate of the Cleveland Oil Company, a Bankrupt.
HICKCOX & CRENSHAW,
Attorneys for Trustee. [6]

United States of America,
Southern District of California,
County of Los Angeles,—ss.

William H. Moore, Jr., being first duly sworn, upon oath says, that he is the objecting trustee in the above-entitled objections to the claim of R. H. Herron Company, and that the facts stated in his foregoing objections to the claim of said R. H. Herron Company are true.

WM. H. MOORE, Jr.

Subscribed and sworn to before me this 23 day of August, 1911.

[Seal] SAMUEL H. PETERS,
Notary Public in and for the County of Los Angeles, State of California.

[Endorsed]: No. 686. In the United States District Court, Southern District of California, Southern Division. In Bankruptcy. In the Matter of the Cleveland Oil Company, a Bankrupt. Objections to Claim of R. H. Herron Company. Filed Aug. 23, 1911, at 2 P. M. Lynn Helm, Referee. Hickcox & Crenshaw, 712–715 Merchants Trust Bldg., 207 South Broadway, Los Angeles, California, Attorneys for Trustee. [7]

[Petition to U. S. District Court for Review of Order of Referee Disallowing Claim.]

In the District Court of the United States, Southern District of California, Southern Division.

No. 686.

In the Matter of the CLEVELAND OIL COMPANY, a Corporation,

Bankrupt.

To the Honorable OLIN WELLBORN, Judge of the District Court of the United States for the Southern District of California.

The petition of the R. H. Herron Company, a corporation organized and existing under the laws of the State of California, one of the creditors of said bankrupt, respectfully represents that on the 3d day of October, 1912, manifest error to the prejudice of complainant, was made by the referee of said matter in a finding and order disallowing and expunging the claim of said corporation against said bankrupt from the list of allowed claims upon the Trustee's

record in said case; and in ordering that the claim of the said R. H. Herron Company for the sum of $14,804.32, as verified and filed with said Referee, be not allowed unless said claimant should surrender and pay to the Trustee of said bankrupt the sum of $5,123.37, together with interest on the sum of $2,000.00, at the rate of seven per cent per annum from the 15th day of September, 1910; interest on the sum of $2,823.37 at the rate of seven per cent per annum from the 31st day of October, 1910; and interest on the sum of $300.00 at the rate of seven per cent per annum from the 31st day of December, 1910.

The errors complained of are:

FIRST.—That the evidence adduced before said Referee at the hearing of the objections made to the allowance of the said claim so presented by the said R. H. Herron Company [8] against the estate of said bankrupt shows that no preference was received by said corporation.

SECOND.—Said Referee erred in finding that the said R. H. Herron Company had reasonable cause to believe that it was intended thereby to give a preference to it by the payment of said sum in the amounts and at the times above stated.

THIRD.—Said Referee erred in finding from the evidence that the said R. H. Herron Company received any preference by reason of said payments above referred to, or either of them.

FOURTH.—Said Referee erred in finding that any payments made to said corporation by said bankrupt were preferences for any amount.

FIFTH.—Said Referee erred in ordering said

corporation to pay the sum of $5,123.37, or any sum at all, to the Trustee before its said claim for $14,-804.32 be allowed.

SIXTH.—Said Referee erred in his conclusions of law from the evidence at said hearing.

WHEREFORE, the R. H. Herron Company prays that it may be decreed by the Court to have its claim against the said bankrupt estate allowed for the full amount thereof, and that it be restored to all things lost by reason of the finding and order of the Referee in said matter.

R. H. HERRON COMPANY,
By GEO. E. WHITAKER,
Its Attorney. [9]

United States of America,
Southern District of California, Southern Division,
County of Los Angeles,—ss.

I, J. M. Sands, do depose and say: That I am the Vice-president, Treasurer and General Manager of the R. H. Herron Company, the petitioner mentioned and described in the foregoing petition, and do hereby make a solemn oath that the statements therein are true according to the best of my knowledge, information and belief.

JOHN M. SANDS.

Subscribed and sworn to before me this 12th day of October, 1912.

[Seal] JACOB B. KISSINGER,
Notary Public in and for the County of Los Angeles, State of California.

My commission expires Jan. 5, 1916.

[Endorsed]: No. 686. In the District Court of the United States, Southern District of California, Southern Division. In the Matter of the Cleveland Oil Company, a Corporation, Bankrupt. Petition to Review Order of Referee Disallowing Claim. Filed Oct. 12, 1912, at 10 o'clock, A. M. Lynn Helm, Referee. Geo. E. Whitaker, Stoner Block, Bakersfield, Cal., Attorney for R. H. Herron Co. **[10]**

Summary of Debts and Assets.

(From the Statements of the Bankrupt in Schedules A and B.)

Schedule A..1 (1)	Taxes and debts due United States		
" A..1 (2)	Taxes due States, Counties, Districts and Municipalities		
" A..1 (3)	Wages...		
" A..1 (4)	Other debts preferred by law.....		
" A..2	Secured claims	$103,271.02	
" A..3	Unsecured claims ...	34,234.61	
" A..4	Notes and bills which ought to be paid by other parties thereto...		
" A..5	Accommodation paper		
	Schedule A, total..		$137,505.63
Schedule B..1	Real estate		$100,000.00
" B..2–a	Cash on hand.....		
" B..2–b	Bills, promissory notes and securities		

Schedule	B..2–c	Stock in trade.....
"	B..2–d	Household goods, etc.
"	B..2–e	Books, prints and pictures .....
"	B..2–f	Horses, cows and other animals.....
"	B..2–g	Carriages and other vehicles ....
"	B..2–h	Farming stock and implements .. ....
"	B..2–i	Shipping and shares in vessels.... ....
"	B..2–k	Machinery, tools, etc..
"	B..2–l	Patents, copyrights and trademarks ..
"	B..2–m	Other personal property .....
"	B..3–a	Debts due on open account... ....
"	B..3–b	Stocks, negotiable bonds, etc. .....
"	B..3–c	Policies of insurance.
"	B..3–d	Unliquidated claims..
"	B..3–e	Deposits of money in in banks and elsewhere .. ..
"	B..4	Property in reversion, remainder, trust, etc..... ....

Schedule B..5 Property claimed to be excepted .....

" B..6 Books, deeds and papers ....

Schedule B, total..$100,000.00

EDSON FRANCE,
Vice-Prest. Cleveland Oil Co.,
Petitioner. [11]

Schedule A—Statement of All Debts of Bankrupt.

SCHEDULE A (1).

Statement of all Creditors Who are to be Paid in Full or to Whom PRIORITY IS SECURED by law.

Dollars. Cents.

(1) TAXES AND DEBTS DUE AND OWING TO THE UNITED STATES—CLAIMS WHICH HAVE PRIORITY.

Reference to Ledger or Voucher. Names of Creditors — Residence (if unknown, that fact must be stated). Where and when contracted. Nature and consideration of the debt, and whether contracted as a partner or joint contractor; and if so, with whom.

(2) TAXES DUE AND OWING TO THE STATE OF..... OR TO ANY COUNTY,

DISTRICT OR MUNICIPALITY THEREOF.

Reference to Ledger or Voucher. Names of Creditors. Residence (if unknown, that fact to be stated). Where and when contracted. Nature and consideration of the debt, and whether contracted as a partner or joint contractor; and if so, with whom.

(3) WAGES DUE WORKMEN, CLERKS OR SERVANTS TO AN AMOUNT NOT EXCEEDING $300 EACH, EARNED WITHIN THREE MONTHS BEFORE FILING THIS PETITION.

Reference to Ledger or Voucher. Names of Creditors. Residence (if unknown, that fact to be stated). Where and when contracted. Nature and consideration of the debt, and whether contracted as a partner or joint contractor; and if so, with whom.

(4) OTHER DEBTS HAVING PRIORITY BY LAW.

Reference to Ledger or Voucher. Names of Creditors. Residence (if unknown, that fact

to be stated). Where and when contracted. Nature and consideration of the debt, and whether contracted as a partner or joint contractor; and if so with whom.

Total.....

EDSON FRANCE,
Vice-Prest. Cleveland Oil Co.,
Petitioner. [12]

SCHEDULE A (3).

CREDITORS WHOSE CLAIMS ARE UNSECURED.

(N. B.—When the Name and Residence (or Either) of any Drawer, Maker, Endorser or Holder of any Bill, or Note, etc., are Unknown, the Fact Must be Stated, Also the Name and Residence of the Last Holder Known to the Debtor. The Debt Due to Each Creditor Must be Stated in Full, and Any Claim by Way of Setoff Stated in the Schedule of Property.)

Dollars. Cents.

Reference to Ledger or Voucher. Names of Creditors. Residence (if unknown, that fact must be stated). When and where contracted. Nature and consideration of the debt, and whether any judgment, bond, bill of exchange, promissory note, etc., and whether contracted as partner or joint contractor with any

other person; and if so, with whom.

All of the following items were taken from the Report of the Mushet Audit Company, which company made an examination of the books of the Cleveland Oil Company as of September 30, 1910.

Alma Oil Company, Bakersfield, Cal.	$ 8.95
Associated Supply, San Francisco, Cal.	1,418.46
Axelson Machine Co., Los Angeles, Cal.	707.08
Bakersfield Iron Works	241.21
Bakersfield Hardware Co.	57.05
Bennett & Robinson	17.00
Bird, H. F.	26.75
Braun Chemical Company, Los Angeles, Cal.	7.20
Bucker Engraving Company, Los Angeles, Cal.	42.12
California Engraving Company, Los Angeles, Cal.	39.95
California Market Company, Bakersfield, Cal.	40.75
Chanslor Canfield Midway Oil Co.	79.50
Cheney, H., Bakersfield, Cal.	198.34
Cooms, L. D., Bakersfield, Cal.	100.00
D. & B. Pump & Supply Company, Los Angeles, Cal.	55.00
Fairbanks Morse & Company, Los Angeles, Cal.	.36
France, W. A., Columbus, Ohio	1,460.84
Goode, O. P.	330.86
Gray, J. E.	180.00

Grimes-Stassforth Stationery Co., Los Angeles, Cal.	15.50
Hale-McLeod Oil Company, Los Angeles, Cal.	21.85
Hawaiian Oil Company	555.25
Hayden Furniture Company, Bakersfield, Cal.	33.00
Heard & Painter	355.85
Hereford Furniture Company	14.50
Hackhenner & Company, Bakersfield, Cal.	3.60
Homes Supply Company, Los Angeles, Cal.	573.56
I. X. L. Blacksmith Shop, Bakersfield, Cal.	4.25
Kern County Abstract, Bakersfield, Cal.	24.90
Kern County Tel. & Tel. Co., Bakersfield, Cal.	13.75
King Lumber Company, Bakersfield, Cal.	97.38
La Bell Oil Company, Los Angeles, Cal.	187.50
Lacy, John, Bakersfield, Cal.	6.50
Leahy, J. F.	8.19
Lucy, J. F., Los Angeles, Cal.	3.10
McDougal Bros.	8.50
McMaster, C. W.	13.95
MacMurdo, W. R.	12.50
[13]	
Midway Fishing Tool Co., Moron, Cal.	120.00
Mission Pharmacy	2.50
Moron Boiler Shop, Moron, Cal.	160.00
Moron Lumber Company, Moron, Cal.	25.60
National Supply Company, Los Angeles, Cal.	7,736.59

Ogden, Lue	16.90
O'Reilley & Brown, Bakersfield, Cal.	163.45
Pacific Coast Mfg. Company, Los Angeles, Cal.	791.50
Parsons & Barton	44.00
Phoenix Ref., Bakersfield, Cal.	35.95
Postal Tel. & Tel. Co., Bakersfield, Cal.	12.41
Total	16,073.95

EDSON FRANCE,
Vice-Pres. Cleveland Oil Co.,
Petitioner. [14]

CREDITORS WHOSE CLAIMS ARE UNSECURED.

(N. B.—When the Name and Residence (or Either) of Any Drawer, Maker, Endorser or Holder of Any Bill or Note, etc., are Unknown, the Fact Must be Stated, and Also the Name and Residence of the Last Holder Known to the Debtor. The Debt Due to Each Creditor Must be Stated in Full, and Any Claim by Way of Setoff Stated in the Schedule of Property.)

Reference to Ledger or Voucher. Names of Creditors. Residence (if unknown, that fact must be stated). When and where contracted. Nature and consideration of the debt, and whether any judgment, bond, bill of exchange, promissory note, etc., and whether contracted as partner or	Dollars.	Cents.

joint contractor with any other person; and if so, with whom.

Forward.....	16,073.95
Ross & Reilley.....	49.30
Silver & Kaar, Bakersfield, Cal.....	102.75
Sprague, F. E. & Bros.	92.00
Standard Oil Company, Fresno, Cal.....	304.27
Stratton Water Company, Fellows, Cal...	773.92
Union Oil Company, Los Angeles, Cal...	763.81
Union Tool Company, Los Angeles, Cal...	65.25
United Veg. Co.....	26.45
Wallace Pump Works.....	52.00
Wood Bros. Transfer.....	32.00
Total.....	18,335.70

BILLS PAYABLE:

Merchants Bank & Trust Co., Los Angeles, Cal.....	5,000.00
Citizens National Bank, Los Angeles, Cal.....	5,352.68
California National Supply, Los Angeles, Cal.....	3,723.91
King Lumber Company, Bakersfield, Cal.	322.32
Total.....	14,398.91
Spicer, C. C. and Sweet, Geo. T., Los Angeles, Cal.....	1,000.00
Batchelder, Wm. J., Los Angeles, Cal....	500.00
Total.....	34,234.61

EDSON FRANCE,
Vice-Prest. Cleveland Oil Co.,
Petitioner. [15]

SCHEDULE A (4).

LIABILITIES ON NOTES OR BILLS DISCOUNTED WHICH OUGHT TO BE PAID BY THE DRAWERS, MAKERS, ACCEPTORS OR INDORSERS.

N. B.—The Dates of the Notes or Bills, and When Due, With the Names, Residences and the Business or Occupation of the Drawers, Makers or Acceptors Thereof, are to be Set Forth Under the Names of the Holders. If the Names of the Holders are not Known, the Name of the Last Holder Known to the Debtor Shall be Stated, and His Business and Place of Residence. The Same Particulars as to Notes or Bills, on Which the Debtor is Liable as Indorser.

Reference to Ledger or Voucher. Names of holders so far as known. Residence, (if unknown, that fact must be stated). Place where contracted. Nature of liability, and whether contracted as partner or joint contractor with any other person; and if so, with whom.	Dollars.	Cents.
Total....		

EDSON FRANCE,
Vice-Prest. Cleveland Oil Co.,
Petitioner. [16]

SCHEDULE A (2).

CREDITORS HOLDING SECURITIES.

(N. B.—Particulars of Securities Held, With Dates of Same, and When They were Given, to be Stated Under the Names of the Several Creditors, and Also Particulars Concerning Each Debt, as Required by the Acts of Congress Relating to Bankruptcy; and Whether Contracted as Partner or Joint Contractor With Any Other Person, and if so, With Whom.)

Reference to Ledger or Voucher. Names of Creditors. Residence (if unknown, that fact must be stated). Description of securities. When and where debts were contracted. Value of securities.	Dollars. Cents.
Merchants Bank & Trust Company, Trustee, first mortgage bonds	$83,500.00
M. J. Monnette, note bearing date October 18, 1909, upon which there remains unpaid	4,997.53
The above obligation is secured by $10,000 in first mortgage bonds	
All of the above figures are taken from the Report of the Mushet Audit Company, which company audited the books of the Cleveland Oil Company as of September 30, 1910.	
R. H. Herron & Company; account se-	

cured by $5,000 in first mortgage bonds..... 14,773.49

This is the amount stated by the R. H. Herron Company as owing to them; we have no means of ascertaining its correctness.

Total.....$103,271.02

EDSON FRANCE,
Vice-Prest. Cleveland Oil Co.,
Petitioner. [17]

SCHEDULE A (5).

ACCOMMODATION PAPER.

N. B.—The Dates of the Notes or Bills, and When Due With the Names and Residences of the Drawers, Makers and Acceptors Thereof, are to be Set Forth Under the Names of the Holders. If the Bankrupt be Liable as a Drawer, Maker, Acceptor or Indorser Thereof, It is to be Stated Accordingly. If the Names of the Holders are not Known, the Name of the Last Holder Known to the Debtor Should be Stated, With His Residence. Same Particulars as to Other Commercial Paper.

Reference to Ledger or Voucher. Name of holders. Residence (if unknown that fact must be be stated). Names and residences of persons accommodated. Place where contracted. Whether liability was contracted	Dollars.	Cents.

as partner or joint contractor, or with any other person; and if so, with whom.

Total.....

EDSON FRANCE,
Vice-Prest. Cleveland Oil Co.,
Petitioner.

OATH TO SCHEDULE A.

United States of America,
Southern District of California,—ss.

On this 16th day of March, A. D. 1911, before me, personally came Edson France, Vice-Pres. Cleveland Oil Company, the person mentioned in and who subscribed to the foregoing Schedule, and who, being by me first duly sworn, did declare the said Schedule to be a statement of all debts, in accordance with the acts of Congress relating to Bankruptcy.

[Seal] CHARLES CLYDE SPICER,
Notary Public in and for the County of Los Angeles, State of California. (Official Character.) [18]

Schedule B—Statement of All Property of Bankrupt.

SCHEDULE B (1).

REAL ESTATE.

	Dollars.	Cents.
Location and description of all real estate owned by debtor, or held by him. Incumbrances thereon, if any, and dates thereof. Statement of particulars relating thereto.		
10 acres owned in fee;		

15 acres leased from the Volcan Oil Company at 25% royalty;
25 acres leased from the California Kern Oil Company at 16–⅔% royalty: All being in the North Half (N. ½) of Section Eight (8), Township Twenty-nine (29) South, Range Twenty-eight (28) East, M. D. B. & M., Kern County, California, together with buildings, machinery, oil drilling equipments, casing, tools and oil on hand..... $100,000.00

All of the above property is subject to a mortgage and bond issue of $100,000, of which bonds $83,500 are outstanding and an additional $15,000 in bonds are in the hands of creditors as collateral security as shown by Schedule A (2)

Total.... $100,000.00

EDSON FRANCE,
Vice-Prest. Cleveland Oil Co.,
Petitioner. [19]

SCHEDULE B (2).
PERSONAL PROPERTY.

		Dollars.	Cents.
A.	Cash on hand.....		
B.	Bills of Exchange promissory notes, or securities (each to be set out separately).....		

C. Stock in trade in ——— business of at ——— of the value of..

D. Household goods and furniture, household stores, wearing apparel and ornaments of the person, viz.... ....

Total....

EDSON FRANCE,
Vice-Prest. Cleveland Oil Co.,
Petitioner. [20]

SCHEDULE B (2) CONTINUED.
PERSONAL PROPERTY.

Dollars. Cents.

E. Books, prints and pictures, viz.

F. Horses, cows, sheep and other animals (with number of each), viz.

G. Carriages and other vehicles, viz.

H. Farming stock and implements of husbandry, viz.

Total.....

EDSON FRANCE,
Vice-Prest. Cleveland Oil Co.,
Petitioner. [21]

SCHEDULE B. (2) CONTINUED.
PERSONAL PROPERTY.

Dollars. Cents.

I. Shipping and shares in vessels, viz:

K. Machinery, fixtures, apparatus and tools used in business, with the place where each is situated, viz.

All machinery, fixtures and tools owned by the company are situated on the real estate described in Schedule B (1).

L. Patent, copyrights and trademarks, viz.

M. Goods or personal property of any other description, with the place where each is situated, viz.

Total.....

EDSON FRANCE,
Vice-Prest. Cleveland Oil Co.,
Petitioner. [22]

SCHEDULE B (3).
CHOSES IN ACTION.

Dollars. Cents.

A. Debts due petitioner on open account.

B. Stock in incorporated companies, interest in joint stock companies, and negotiable bonds.

C. Policies of Insurance.

D. Unliquidated Claims of every nature with their estimated value.

E. Deposits of money in banking institutions and elsewhere.

Total.....

EDSON FRANCE,
Vice-Prest. Cleveland Oil Co.,
Petitioner. [23]

SCHEDULE B (4).

PROPERTY IN REVERSION, REMAINDER OR EXPECTANCY, INCLUDING PROPERTY HELD IN TRUST FOR THE DEBTOR, OR SUBJECT TO ANY POWER OR RIGHT TO DISPOSE OF OR TO CHARGE.

N. B.—A Particular Description of Each Interest must be Entered, if All, or Any of the Debtor's Property has been Conveyed by Deed of Assignment or Otherwise, for the Benefit of Creditors, the Date of Such Deeds Should be Stated, the Name and Address of the Person to Whom the Property was Conveyed, the Amount Realized from the Proceeds Thereof, and the Disposal of the Same, as far as Known to the Debtor.

General Interest.	Particular Description.	Supposed Value of my Interest. Dollars.	Cents
Interest in land.			
Personal property.			
Property in money, stocks, shares, bonds, annuities, etc.			
Rights and powers, legacies and bequests.			
Total.....			

Property Heretofore Conveyed for the Benefit of Creditors.	Amount Realized from Proceeds of Property Conveyed.
What portion of debtor's property has been conveyed by deed of assignment, or otherwise, for benefit of creditors; date of such deed, name and address of party to whom conveyed; amount realized therefrom, and disposal of same, so far as known to debtor.	
What sum or sums have been paid to counsel, and to whom for services rendered or to be rendered in this bankruptcy.	
Total....	

EDSON FRANCE,
Vice-Prest. Cleveland Oil Co.,
Petitioner. [24]

SCHEDULE B (5).

A Particular Statement of the Property Claimed as Exempted from the Acts of Congress Relating to Bankruptcy, Giving Each Item of Property and Its Valuation; and if Any Portion of It is Real Estate, Its Location, Description and Present Use.

	Dollars.	Cents.
Military uniforms, arms and equipments.		
Property claimed to be exempted by State Laws; its valuation; whether real or personal; its de-		

scription and present use; and reference given to the statute of the State creating the exemption.

Total....

EDSON FRANCE,
Vice-Prest. Cleveland Oil Co.,
Petitioner. [25]

SCHEDULE B (6).

BOOKS, PAPERS, DEEDS AND WRITINGS RELATING TO BANKRUPT'S BUSINESS AND ESTATE.

The following is a true list of all books, papers, deeds and writings relating to my trade, business dealings, estate and effects, or any part thereof, which at the date of this petition, are in my possession, or under my custody and control, or which are in the possession or custody of any person in trust for me, or for my use, benefit or advantage; and also of all others which have been heretofore, at any time, in my possession or under my custody or control, and which are now held by the parties whose names are hereinafter set forth, with the reason for their custody of the same.

Books:

Deeds:

Papers:

EDSON FRANCE,
Vice-Prest. Cleveland Oil Co.,
Petitioner.

OATH TO SCHEDULE B.

United States of America,
Southern District of California,—ss.

On this 16th day of March, A. D. 1911, before me, personally came Edson France, Vice-Pres. of Cleveland Oil Co., the person mentioned in and who subscribed to the foregoing schedule and who, being by me first duly sworn, did declare the said Schedule to be a statement of all estate, both real and personal, in accordance with the Acts of Congress relating to bankruptcy.

[Seal] CHARLES CLYDE SPICER,
Notary Public in and for the County of Los Angeles, State of California.
(Official Character.) [26]

[Endorsed]: No. 686 — Bankruptcy. United States District Court, Southern District of California, Southern Division. In the Matter of Cleveland Oil Company, Bankrupt. Petition by Debtor With Schedules A and B. (Schedules must be Filed in Triplicate.) Filed Mar. 22, 1911, at 10 min. past 3 o'clock P. M. E. H. Owen, Clerk. C. E. Scott, Deputy. Charles Clyde Spicer, Attorney for Petitioner. [27]

[Trustee's Exhibit No. 3.]

AN AMERICAN PAPER FOR THE AMERICAN PEO——

—— ANGELES (CUT) EX——

LOS ANGELES, DECEMBER 20, 1910.

DIVIDENDS EXCEED PROFITS BY $6500.

FACT CLEVELAND OIL CO. STOCKHOLDERS COULDN'T UNDERSTAND VERIFIED BY EXPERT.

LAX METHODS CHARGED.

MEN SERVING AS DIRECTORS WITHOUT AUTHORITY AMONG ILLEGAL ACTS CLAIMED.

A detailed report on the affairs of the Cleveland Oil Company, whose preparation followed the demands of dissatisfied stockholders for an investigation, was made public yesterday and presented an astonishing narrative of lax methods.

The report, which was compiled by W. C. Mushet, an expert accountant, was read yesterday to about 150 stockholders, who met in one of the Stock Exchange rooms. It comprises more than fifty typewritten pages and goes exhaustively into the history of the company.

The fact which seemed to impress the stockholders as most significant was that there were two payments of dividends aggregating more than $9000 in ten months, whereas the profits of the company during that time were about $2500.

USE STOCK TO PAY DIVIDENDS.

As dividends, according to legal regulations, can only be paid from profits, it appears, and the report so states, that the directors of the Cleveland Oil Company paid a considerable sum from the sale of stock for this purpose. [28]

The mismanagement or lack of management extended over a long period, according to the report. Men served as directors who had never been elected as such, and there were instances cited where only two directors had taken important action with respect to the business of the concern.

The records of the issues of stock were not in keeping with legal requirements and the report showed that the stock books did not check up with the amount of stock disposed of.

Several officers of the company had stock accounts with the company and were in possession of stock that had not been paid for. This condition had been permitted by the directors, said the report.

INVESTORS DISCONTENTED.

The origin of yesterday's expose was the insistence of stockholders about two months ago that the company be investigated. Their discontent arose over the fact that no dividends had been paid recently, although the reports indicated that the company was producing oil.

The chairman of the stockholders' meeting appointed five men who, in turn, engaged the services of the expert accountant. Requests have been made from time to time that the report be produced, but

it was not until yesterday that the stockholders knew all the facts.

At one time the stock was selling on the exchange as high as 55 cents a share. The last quotation was $10 per 1,000 shares. [29]

[In pencil:] H—Calu 1260

12–20–1910.

MINING A——

AUDITOR FINDS FRAUD IN CLEVELAND AFFAIRS.

OIL COMPANY WRECKED BY PROMOTERS REFUS*ES* TO REPORT TO VICTIMS AND IS EXPOSED.

The affairs of the Cleveland Oil Company under examination by expert accountants, prove to be in a deplorable condition, with scarcely anything favorable for the stockholders and with the stamp of fraud and dishonesty in evidence throughout. A report of the stock exchange committee read yesterday at the close of the call showed that the Cleveland's accounts were inaccurate, its prospectus untrue, that it had paid in dividends more than its earnings, and that among other discrepancies its directors had made over to themselves large blocks of stock at a very low price.

The committee's report was made possible only after the exchange had been put to a great deal of trouble.

The Cleveland directors were, the committee states, to report as far back as October 1 on the affairs of

the company. But they failed to do so. Then several other dates were set and ignored by the Cleveland people. Finally one day last week was set for the report, but the Cleveland people did not show up.

The meeting yesterday was open to the public and was called by Edward Grak, a Cleveland stockholder, who said the stockholders had been kept in the dark and unshed light. Don Dickinson of the exchange was appointed chairman, and Charles P. Sutton secretary. The report of the investigation committee was read by Broker Sullivan. [30]

Mr. Sullivan said the committee appointed the Mushet Auditing Company to examine and report on the books of the Cleveland. He read from this report excerpts showing where the Cleveland was in bad financial and moral condition. The prospectus was first picked to pieces and found, said the auditing company, "inaccurate." Here the production was set at 300 barrels daily in November. Mr. Mushet showed by the books where the ten months preceding July, 1910, gave a total production of only 8000 barrels after royalty was deducted.

The next head in the report covered "assignments to the Cleveland Oil Company by its directors" of leases and so forth. W. A. France, was frequently mentioned in these assignments and involved large blocks of stock, in payment therefor, at 15 cents a share.

ORDERED TO VACATE.

The report then showed where the leases were forfeited and the Cleveland was ordered to vacate its

Kern river property for failure to live up to its contracts of development and payment of royalty.

At a meeting of directors of the Cleveland, the report stated, business of the company was turned over to two lone members of the board, namely, T. M. Montgomery and W. J. Bachelder. France and his associates withdrew on plea that business demanded their presence elsewhere.

The minutes of following meetings revealed the fact that there was frequent transfers of stock showing also where treasury stock had been donated contrary to law. At one of these strange meetings, attended by the two lone directors, it was moved by Montgomery and seconded by Bachelder that Montgomery take charge of the plant in the field at $200 a month and receive 10,000 shares of stock for the privilege of serving his own company. [31]

The question of Cleveland dividends was next discussed in the report. "Were the dividends paid from earnings or from capital?" is the head of this chapter.

The report showed that two dividends were paid, amounting to $9641. Receipts were $13,000, expenses $4999, and gross receipts $8000. That the gross receipts were not sufficient for dividends was emphasized in the report.

Bills fell due with no money to pay them. It was then that the moving spirits of the company had to dig up $25,000. In a quiet meeting of directors it was reported that G. G. Gillette, former vice-president of the Cleveland; W. A. France, its president, and Secretary Bachelder offered to "loan" the com-

pany on promise of stock and bonds therein the sum of $25,000. The "loan" was made in September, 1910, says the Mushet report. [32]

[Endorsed]: Cleveland Oil Co. U. S. District Court. No. 686. Trustee ——'s Exhibit No. 3. Filed July 25, 1912. Helm, Referee. [33]

[Trustee's Exhibit No. 4.]

OIL OFFICIAL ARRESTED.

T. M. MONTGOMERY OF CLEVELAND COMPANY BROUGHT TO CITY FROM BAKERSFIELD.

MISUSE OF MAILS CHARGE.

Thomas M. Montgomery, treasurer of the Cleveland Oil Company, was brought to this city today in charge of Bert Franklin, deputy United States marshal, from Bakersfield, where he was arrested, charged with using the mails in a scheme to defraud.

He was taken into custody in connection with the alleged swindling operations of the promoters of the concern, which was raided last Wednesday, when W. J. Batchelder and G. G. Gillette were arrested.

Montgomery was arraigned before William M. Van Dyke, United States Commissioner, and furnished $5000 bail to appear for an examination Dec. 30, the same date set for the hearing of testimony respecting the operations of Gillette and Batchelder.

FOUND ON HUNTING TRIP.

Montgomery and a party of friends were on a hunting trip at a lake 30 miles west of Bakersfield,

and Deputy Marshal Franklin drove 72 miles in an automobile yesterday and followed the gun shots of hunters around the shores of the lake until late in the afternoon before finding his man.

The arrests are part of a plan on the part of the Government to eliminate stock jobbing concerns under a new law recently passed.

This new act prohibits the sending through the mails of any literature or information respecting companies promoted for purposes of fraud. [34]

NEW RULING ON MAILS.

Formerly it was necessary that the letters in question should convey false intelligence before the Government could take a hand in the matter. Now, however, if fraud can be proved against the officers of the company, any information respecting the concern or its operations, whether true or not, is barred from the mails.

The Cleveland Oil Company was made defendant in a civil suit filed today in the Superior Court by William Button to recover on a note for $5352.68, signed by W. C. France, as president; W. J. Batchelder, as secretary, and Thomas M. Montgomery, as treasurer.

From Los Angeles Express December 23rd, 1910.

[Endorsed]: U. S. District Court. No. 686. Trustee Exhibit No. 4. Filed July 25, 1912. Helm, Referee. [35]

[Trustee's Exhibit No 5.]

Los Angeles, California, October 18th, 1910.

Mr. J. O. Scott, District Manager,
Taft, California.

Dear Sir:

The Cleveland Oil Company owe us considerable money and they are not in position to supply the ready cash. Their stock is almost worthless from a stock market view, the last sales being passed at 2¾¢. They are endeavoring to arrange the Company on a good financial basis, but that will take some time. They have arranged to deliver us a string of 10″ 40# Casing on the well they are drilling in the Midlands, and we have promised to give them credit when delivered to our stock at Moron, at list less 25%.

The thought occurs to me that the Corrigan Oil Company have to furnish a string of Casing of this size and weight to the Kanawha Oil Company. In view of this make a personal visit to the lease where the Casing is located, inspect it and see if it is such as we could honestly deliver to the Kanawha Oil Co. in accordance with our contract. In that case, you can understand the Corrigan Oil Company would be saving a very considerable hauling charge on the stock they have at McKittrick, and that we can very easily dispose of our stock at McKittrick. In all, it might mean a saving to our Co. of $250 to $300. This conversation I had with Mr. France, who tells me that the name of the man on the lease, is Ware, but he also made mention of a Mr. Becker as being familiar with the conditions on the property. Therefore,

meet one of these gentlemen, inspect the Casing and I will leave it entirely with you as to whether it is Casing that we can deliver to the Kanawaha Oil Co. If it is, have it delivered to their lease instead of to our stocks at Moron, for you understand we buy the Casing delivered.

Yours very truly,

JOHN M. SANDS. [36]

[Endorsed]: U. S. District Court. No. 686. Trustee ——'s Exhibit No. 5. Filed July 25, 1913. Helm, Referee. [37]

[Trustee's Exhibit No. 7.]

Los Angeles, California, August 6th, 1910.

Cleveland Oil Co.

Mr. Geo. W. Church, Manager.

Oil Well Supply Co.,

Bakersfield, California.

Dear Sir:

We have yours of the 5th inst. Communicate with this office before delivering any great amount of goods to the above Company. They are owing us about $20,000.

Yours very truly,

JOHN M. SANDS.

JMS/R.

U. S. District Court. No. 686. Trustee ——'s Exhibit No. 7. Filed July ————. [38]

[Trustee's Exhibit No. 6.]

1260

Los Angeles 9/21/1910.

Cleveland Oil Company.
Mr. J. L. Scott, Division Manager,
Mr. Geo. W. Church, Manager, Bakersfield,
Mr. E. C. Kellermeyer, Manager, Taft,
Mr. H. W. David, Manager, Maricopa,
California.

Gentlemen:

This Company has about all the credit we care to extend them; in fact we don't care to have it increased over $50.00 between the several stores addressed above. The information is sent you so that you may be on your guard and if they should ask for deliveries in excess of this amount, communicate with this office, and those at the Los Angeles in charge of credit, should get the cash before authorizing delivery.

With this communication, all are posted and there is no reason why instructions in connection with this account should miscarry.

Yours very truly,

R. H. HERRON CO.,

Affiliated With the OIL WELL SUPPLY CO. of Pittsburgh, Penn.

JOHN M. SANDS,
Treasurer.

JMS/R.

[Endorsed]: U. S. District Court. No. 686. Trustee ——'s Exhibit No. 6. Filed July 25, 1912. Helm, Referee. [39]

[Notes of Union Oil Co.]

Los Angeles, Cal., May 9, 1910.

[In ink:] 108.

[In pencil:] 9450

$4052.79

[In pencil:] 4147.29.

Four months after date, without grace We promise to pay to the order of R. H. Herron Co. Four thousand Fifty-two.....79/100 Dollars, for Value received, with interest (CUT) from date at the rate of 7 per cent per annum until paid. Principal and interest payable in U. S. GOLD COIN., at 427 H. W. Hellman Bldg. and in case suit is instituted to collect this note or any portion thereof, we promise to pay such additional sum as the Court may adjudge reasonable as Attorney's fees in said suit.

[In red ink:] 8356.

CLEVELAND OIL COMPANY.

W. A. FRANCE,

Pres.

W. J. BATCHELDER,

Aug. 31, 1910. Secy.

No. ——. Due Sept. 10, 1910.

U. S. (Shield) Bond. No. 101.

Stamped across the face of the Note, enclosed within border, and partially blurred, is the following:

Correction PAID SEP 10 1910 FIRST NATION BANK LOS ANGELES CAL

[Endorsed on Back:] Pay to the Order of Oil Well Supply Co. Endorsement Cancelled. R. H. Herron Co. John M. Sands. Endorsement Cancelled Oil Well Supply Co. Louis Brown, Treasurer. Endorsement Cancelled. Pay to the Order of Any Bank, Banker or Trust Co. Aug 26, *19,* the First National Bank of Pittsburgh, Pa. F. H. Richard, Cashier. Collection Department. [40]

[In pencil:] OK. WHL.

[In ink:] 116.

$2868.15.

Los Angeles, California, May 23 —— 1910.

Ninety days after date, without grace we —— promise to pay to the order of (CUT) Ourselves Twenty-eight hundred & sixty eight & 15/100 Dollars, for Value Received, with interest from date at the rate of – 6 – per cent per annum until paid. Principal and interest payable in U. S. GOLD COIN, at Los Angeles California and in case suit is instituted to collect this note or any portion thereof, we promise to pay such additional

sum as the Court may adjudge reasonable as Attorney's fees in said suit.

[Seal] CLEVELAND OIL COMPANY.
By W. A. FRANCE, Pres.
By W. J. BATCHELDER, Secy.

No. 24347 Due 8/21/10.
U. S. (Shield) Bond. No. 101.

[Endorsed on Back]: Cleveland Oil Company by W. A. France, Pres., by W. J. Batchelder, Secy.

For value received, I, R. H. Herron Co., hereby waive presentment, demand, notice, protest and notice of protest and guarantee the payment of this note at maturity.

R. H. HERRON CO.
WALTER H. LYNN,
Secretary. [41]

[In ink:] 143. 7462 int $327293. 4117. Oct. 24 $3,198.31. Los Angeles, Cal., June 23, 1910.

Four months after date, without grace We promise to pay to the order of R. H. Herron Co. Thirty-one Hundred Ninety-eight.....31/100 Dollars, for Value (CUT.) received, with interest from date at the rate of 7 per cent per annum until paid. Principal and interest payable in U. S. GOLD COIN, at ofc. R. H. Herron Co. L. A. and in case suit is instituted to collect this note or any portion thereof, we promise to pay such additional sum as the Court may ad-

judge reasonable as Attorney's fees in said suit.

CLEVELAND OIL CO. 74398
By W. A. FRANCE,
Pres.
W. J. BATCHELDER,
Secy.

[In pencil:] 45.26
24th
No. 5. Due Oct. ~~23~~, 1910.
U. S. (Shield) Bond. No. 101.

Endorsed on face of Note is the following: Enclosed within circle:—capital letter (P). Enclosed within border, stamped:—PAID OCT 24 1910. Collection Dept. CITIZENS NAT'L BANK Los Angeles, Cal.

(Endorsed on back is the following: (54.58. Pay to the Order of the Oil Well Supply Co. Endorsement Cancelled. R. H. Herron Co. John M. Sands, Treasurer. Endorsement Cancelled. Oil Well Supply Co. Louis Brown, Treasurer. Endorsement Cancelled. Pay to the Order of Any Bank, Banker or Trust Co. This and All Prior Endorsements Guaranteed. Coll. No. 17924. The Bank of Pittsburgh N. A. W. F. Bickel, Cashier. Sep. 28, 1910.

[42]

172. $2607.43 Los Angeles, Cal., July 16, 1910.

On November 15th 1910 after date, without grace we or either of us promise to pay to the order of R. H. Herron Co Twenty Six Hundred Seven and 43/100–Dollars, for maturity

Value received, with interest from ~~date~~ at

the rate of seven per cent per annum until paid. Principal and interest payable in U.
(CUT.) S. GOLD COIN., at office R H Herron Co Los Angeles Cal and in case suit is instituted to collect this note or any portion thereof, we promise to pay such additional sum as the Court may adjudge reasonable as Attorney's fees in said suit.

CLEVELAND OIL CO.

[Seal of Cleveland Oil Co.]

By W. J. BATCHELDER, Secy.

A

THOS. M. MONTGOMERY, Treas.

[In pencil:] 115.

[In red ink:] 9218.

No. —— Due Nov. 15–10—29

U. S. (Shield) Bond. No. 101.

(Endorsed across the front of Note, stamped within circle, is the following:)

NOV 15 1910 LOS ANGELES CAL
COMMERCIAL NATIONAL BANK. Collection Dept.

[Endorsed on Back:] Pay to the Order of Oil Well Supply Co. Endorsement Cancelled. R. H. Herron Co. John M. Sands, Treasurer. Endorsement Cancelled. Oil Well Supply Co. Louis Brown, Treasurer. Endorsement Cancelled. Pay First National Bank, Pittsburg, Pa, or order. Previous Endorsements Guaranteed. First National Bank, McKeesport, Pa. Charles A. Tawney, Cashier. 1280. Pay to the Order of Any Bank, Banker or Trust Co.,

Oct. 20, 1910. The First National Bank of Pittsburgh, Pa. F. H. Richard, Cashier. Collection Department. [43]

[Certificate of Clerk U. S. District Court to Supplemental Transcript of Record, etc.]

In the District Court of the United States of America, in and for the Southern District of California, Southern Division.

IN BANKRUPTCY—No. 686.

In the Matter of CLEVELAND OIL COMPANY, a Corporation,

Bankrupt.

I, Wm. M. Van Dyke, Clerk of the District Court of the United States of America, in and for the Southern District of California, do hereby certify the foregoing typewritten pages, numbered from 1 to 43, inclusive, and comprised in one volume, to be a full, true and correct copy of the Proof of Debt filed by the R. H. Herron Company, the Petition for Review of Referee's Report, Trustee's Exhibit 6, being a letter dated September 21, 1910, Trustee's Exhibit 7, being a letter dated August 6, 1910, Trustee's Exhibit 5, being a letter dated October 18, 1910, Trustee's Exhibits 3 and 4, being newspaper clippings, four notices of Cleveland Oil Company to R. H. Herron Company, Summary of Schedules and Schedule B, and Objections of Trustee to the Claim of the R. H. Herron Company, and that the same together with the Transcript on Appeal issued and certified to on February 19, 1913, constitute the Transcript of the Record on Appeal to the [44] United States

Circuit Court of Appeals for the Ninth Circuit, in said cause.

I do further certify that the cost of the foregoing Supplemental Record is $19.70, the amount whereof has been paid me on behalf of said R. H. Herron Company, a corporation.

In testimony whereof, I have hereunto set my hand and affixed the seal of the District Court of the United States of America, in and for the Southern District of California, Southern Division, this 10th day of May, in the year of our Lord one thousand nine hundred and thirteen, and of our Independence the one hundred and thirty-seventh.

[Seal] WM. M. VAN DYKE,
Clerk of the District Court of the United States of America, in and for the Southern District of California.

By Chas. N. Williams,
Deputy Clerk. [45]

[Endorsed]: No. 2254. United States Circuit Court of Appeals for the Ninth Circuit. R. H. Herron Company, a Corporation, Appellant, vs. William H. Moore, Jr., Trustee in Bankruptcy of the Cleveland Oil Company, a Corporation, Appellee. Supplemental Transcript of Record. Upon Appeal from the United States District Court for the Southern District of California, Southern Division.

Filed May 12, 1913.

FRANK D. MONCKTON,
Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

By Meredith Sawyer,
Deputy Clerk.

No. 2254

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT.

R. H. HERRON COMPANY, a Corporation,
Appellant,

vs.

WILLIAM H. MOORE, Jr., Trustee in Bankruptcy of the Cleveland Oil Company, a Corporation,
Appellee.

POINTS AND AUTHORITIES OF THE R. H. HERRON COMPANY, CLAIMANT AND APPELLANT.

STATEMENT OF FACTS

Briefly outlined the facts are as follows:

On the 12th day of January, 1911, an involuntary petition in bankruptcy was filed against the above entitled bankrupt, the Cleveland Oil Company, and on February 20th, 1911, the company

was duly adjudicated a bankrupt upon the said petition.

The R. H. Herron Company after the adjudication filed a claim against the bankrupt estate for the sum of $14,804.32, consisting of an open account for $6376.53 for goods, wares and merchandise sold and delivered by the claimant to the bankrupt and the balance for the sum of $8427.79 and evidenced by four promisory notes made by said bankrupt and due respectively August 21, September 10, October 24 and November 15, 1910.

It appeared that on September 15th, 1910, the bankrupt had paid to the R. H. Herron Company the sum of $2000.00 on account; that on October 31st, 1910, the bankrupt returned to the company certain oil well casing of the value of $2823.37 in part payment of its indebtedness; and that on the 31st day of December 1910, the bankrupt returned to the company two pumps of the value of $300.00 also in part payment of its indebtedness. The trustee in bankruptcy objected to the claim of the R. H. Herron Company on the ground that these payments constituted preferences. The Referee decided that the payment of the $2000.00 and the transfers of the property to the company were all preferences; he found that the claimant had reasonable cause to believe that a preference was intended, and he held that the claim of the company for $14,804.32 be not allowed unless the company surrender to the Trustee the sum of $5123.37 together with interest on the various

sums above mentioned from the time they were credited to the bankrupt by the company. On a review of this report of the Referee by the Hon. Olin Wellborn, District Judge, the finding and decision of the Referee were confirmed.

It is from the decree of the District Court affirming the finding and decision of the Referee that this appeal is prosecuted.

PRELIMINARY CONSIDERATIONS

The sole question for determination here is whether at the time of the payment of the money and the transfer of the property by the Cleveland Oil Company to the R. H. Herron Company, the latter had resasonable cause to believe that the payment or transfers would effect a preference. Payments or transfers within four months from the filing of the petition in bankruptcy are valid unless the creditor receiving them had at the time reasonable cause to believe that they would effect a preference.

This is the express provision of the Bankruptcy Act.

Bankruptcy Act, Section 60b.

It is to be remembered that the creditor **at the time** of the payment or transfer must have had reasonable cause to believe a preference was intended.

In re Onimette, 18 Fed. Cas., 913.

In re Sayed, 26 Am. Bank Rep., 444, 447, S. C. 185 FED., 962.

Hicks v. Longstreet, 6 Am. Bank Rep., 178.

Therefore, the question is whether at the time of the payment and transfers made herein, the R. H. Herron Company had reasonable cause to believe a preference was intended.

In determining this question the rule is firmly settled that the burden of proof is upon the party claiming that the transfers constituted a preference.

"The law presumes that the payments made by "the bankrupt were legal and the burden of "proof is on the trustee to overcome this pre-"sumption."

Starbuck v. Gebo, 48 N. Y. Misc., 333, per Rockwood, J.

"It has never been denied," said Miller, J., "so "far as we are advised that it is necessary for the "assignee of the bankrupt in attacking such a "conveyance to prove the existence of this rea-"sonable cause of belief of the debtor's insolv-"ency in the mind of the preferred party."

Barbour v. Priest, 103 U. S., 293.

This rule is supported by a vast array of authority.

Cullinane v. State Bank, 123 Ia., 340.

Borden v. Dresser, 98 Me., 519.

Halbert v. Pranke, 91 Minn., 204.

Powel v. Gate City Bank, 178 Fed., 609.

Greene v. Montana Brewing Co., 28 Mont., 380.

Upson v. Mt. Morris Bank, 103 N.Y. App. Div., 367.

Jackson v. Valley, etc., Co., 108 Va., 714.
Calhoun Co. Bk. v. Cain, 152 Fed., 983.
Stevens v. Oscar Holway Co., 156 Fed., 90.
In re Leech, 171 Fed., 622.

And the burden is on the Trustee to prove by evidence establishing more than a mere suspicion that the bankrupt intended to prefer a creditor when the payment was made and that the creditor knew or had reasonable cause to believe that such preference was intended.

Reber v. Shulman, 179 Fed., 574, aff'd 183 Fed., 564.

Furthermore this proof to be adduced by the trustee to overthrow an alleged preference must go to the extent of showing that the creditor had reasonable cause to believe **that the debtor was in fact insolvent.**

"Reasonable cause for belief that a preference "was intended to be given necessarily involves "reasonable cause for the belief that the debtor "was in fact insolvent."

1 Remington on Bankruptcy, §1402.

"Merely to establish grounds which reasona- "bly would have caused the creditor to believe "the debtor insolvent is not enough."

Idem, §1403.

"Reasonable cause to believe a preference was "intended involves reasonable cause to believe "the creditor knew insolvency existed as a mat- "ter of fact."

Idem, §1404.

The creditor must have had actual knowledge of the bankrupt's insolvent condition or the circumstances of the case must have been such as to put him upon inquiry and thereby render him chargeable with such knowledge.

In re Houghton Web Co., 26 Am. Bank Rep., 202.

A creditor must have reasonable cause to believe that his debtor is insolvent in fact as a foundation for reasonable cause to believe that an unlawful preference in favor of such ceditor was intended.

Wright v. Cotten, 52 S. E., 141.

And it is not enough that a creditor has some cause to suspect the insolvency of his debtor, but he must have such a knowledge of facts as to induce a reasonable belief of his debtor's insolvency.

Off v. Hakes, 142 Fed., 364.

A creditor "could have no reasonable cause to "believe that a preference was intended unless he "knew or suspected the insolvency of the "debtor."

Hergberg v. Riddle, 54 So. (Ala.) 635, 637, per Mayfield, J.

"To constitute a voidable preference as defined "by §§60a-60b, the creditor must have reasonable "cause to believe the debtor to be insolvent in "fact as a foundation for reasonable cause to be-"lieve that an unlawful preference is intended."

In re Eggert, 3 Am. Bank Rep. 541; S. C. 98 Fed. 843, per Brown, D. J., aff'd 4 Am. Bank Rep. 449, S. C. 102 Fed. 735.

The same rule was affirmed in Des Moines Sav. Bank v. Morgan Jewelry Co., 12 Am. Bank Rep. 781, s. c. 123 Ia. 432, where a mortgage was attacked as being a preference.

Bishop, J., in delivering the opinion in this case said: (pp. 785-786)

"Essential to such a preference is insolvency "because if the debtor was solvent, the execution "of the mortgage would not in all likelihood "operate to defeat the other creditors of the "mortgagor; knowledge or a reasonable cause to "believe that a preference is intended involves "therefore knowledge or a reasonable cause to "believe that insolvency exists as a matter of "fact."

From the foregoing authorities it follows that the burden of proof is on the trustee and that the proof introduced by him must go to the extent of proving that the creditor had reasonable cause to believe that insolvency existed as a matter of fact. When these rules are applied to the case under consideration, no other conclusion can be reached than that the trustee has failed to sustain the burden imposed upon him for there is nothing in the record to sustain the position that the R. H. Herron Company believed or had reason to believe the Cleveland Oil Company was insolvent as a matter of fact.

THE FACT THAT THE CLEVELAND OIL COMPANY WAS SLOW IN ITS PAYMENTS AND THAT ITS CREDIT WAS CUT OFF, EXCEPT FOR EMERGENCY SUPPLIES DOES NOT CHARGE THE R. H. HERRON COMPANY WITH REASONABLE CAUSE TO BELIEVE A PREFERENCE WAS INTENDED.

The Referee below held that the R. H. Herron Company had reasonable cause to believe a preference was intended. This finding, it is respectfully submitted was error.

It was attempted to be shown that the credit of the Cleveland Oil Company was cut off on the last of August, 1910, (Tr. p. 73, lines 16 and 17.) This fact was not proven by the Trustee for it appears the company was privileged to call at the Bakersfield store of the R. H. Herron Company and buy supplies for emergency requirements; if it wanted anything in excess of the emergency requirements, it was to communicate with the Los Angeles office of the company.

(Transcript, p. 73, lines 22-27.)

Under any circumstances the mere facts that the Cleveland Oil Company was slow in its payments, that it was unable to pay its debts promptly and that in consequence its credit was curtailed, or even cut off, would not charge the creditor with having reasonable cause to believe a preference was intended.

"Neither the mere non-payment of the par"ticular creditor's claim nor the fact that most of

"the indebtedness to the creditor is past due at "the time of the payment on account and that "the creditor has been urging payment and the "debtor repeatedly promising it, is in itself suf "ficient cause for drawing the inference."

1 Remington on Bankruptcy, §1409.

This doctrine has been frequently applied.

Thus in In re Goodhile, 12 Am. Bank Rep. 374, it was held that the fact that most of the bankrupt's indebtedness to a creditor was past due at the time of a payment on account within the four month's period was not sufficient to charge the creditor with reasonable cause to believe that the bankrupt was insolvent within the meaning of the bankrupt act and that a preference was intended so as to bar proof of the creditor's claim because such payment had not been surrendered.

It appeared here that the creditor was urging payment and that the debtor was promising to pay as fast as she could. There were no other facts from which it could be inferred that the debtor was in an insolvent condition or intended a preference. It was held that the referee erred in rejecting the claim.

"A creditor may suspect his debtor of in- "solvent circumstances, but he may not have suf- "ficient evidence thereof so as to justify him in "refusing to receive payment of his debt in peril "of violating the bankruptcy law. The cases hold "that he may be even unwilling to trust him "further. He may become anxious about his

"claim and desire security for it. Additional "security and receiving payments under such "circumstances are not prohibited by law."

Harder v. Clark, 66 Misc. (N. Y.) 584, 585, per McAvoy, J.

The fact that a creditor demands and receives from his debtor security for a previously unsecured debt at a time when the debtor was actually insolvent does not create an inference that the creditor knew of such insolvency or had reasonable grounds for believing that the transfer was made with intent to create a preference.

Perry v. Booth, 80 N. Y. App. Div. 373.

In the case under consideration there was no fact to show that the Cleveland Oil Company was insolvent, except the fact that it was not able to pay its debts. Therefore the language of Jenkins, J., in In re Eggert, 102 Fed. 735, is directly applicable. In this case in discussing a similar question the learned Judge said: (p. 742)

"The only fact brought home to the creditor "and which it is claimed should have aroused in- "quiry is that he was somewhat behind in the "prompt payment of his obligation. We cannot "say, as a conclusion of law, that knowledge of "that fact standing alone was sufficient to put the "creditor upon inquiry. Indeed, it may be said "that a majority of merchants absolutely solvent "in the sense in which the term is employed in "the bankruptcy act, are not at all times able to "meet the obligations as they mature. To hold

"that a creditor receiving payment of or security "for a debt past due is, by the mere fact of knowl- "edge that the debt is past maturity put upon "inquiry of his debtor's inability to pay all his "debts and that under such circumstances he re- "ceived payment or security at his peril, would "be to put at hazard many business transactions "and make the act oppressive. The fact of such "inability, coupled with other facts and circum- "stances brought home to the creditor might put "him on inquiry; but this is the only fact from "which the deduction is sought that the creditor "had reasonable cause to believe his debtor in- "solvent, and standing alone, it is insufficient to "raise an inference of law that the creditor is "chargeable with knowledge of the facts which "inquiry would have elicited."

As has been noticed there is not a shred of testimony in the record to show the creditor's knowledge of the state of affairs other than the single fact the debtor was behind in its payments. This language then applies with full force and clearly shows that no reasonable cause was proven.

In the case of In re Ebert, 2 Am. Bank Rep. 340, it appeared that a creditor could not obtain his money and hired an attorney to collect it. The debtor gave security. The debtor firm was shaky but the partners thought it could pull through. There was nothing to impeach the good faith of the creditor and he did not know of the shaky

condition of the firm. It was held that there was no preference.

That a creditor's knowledge of the debtor's inability to meet his obligation does not show reasonable cause has found frequent illustration in the authorities.

Thus the mere fact that an involuntary bankrupt within the four month's period deposited with a creditor certain book accounts to secure his obligation is not sufficient to show that the creditor had reasonable cause to believe that the securing of its claim was intended as a preference.

> Laundy v. First Nat. Bank, 11 Am. Bank Rep. 223.

And a loan to a bankrupt to extricate himself may be made without violating the provisions of the bankrupt law.

> Darby v. Boatmans Sav. Ins, I Dillon, 142. s. c. on appeal 18 Wallace, 375.

The same rule was laid down in Casey v. La Soirete, etc., Co., 2 Woods 77 and in In re Kullberg, 23 Am. Bank Rep. 758, s. c. 176 Fed. 585.

In Smith v. Hewlett Robin Co., 24 Am. Bank Rep. 153, where an offer of compromise was made, it was held that creditors were justified in believing that it was made in good faith to all the creditors and unless something occurred to put them on inquiry, in the absence of which it was not their duty to investigate to ascertain if the debtor could pay the amount offered and intended

to pay it to all the creditors alike. In this case the Trustee in bankruptcy sought to recover the sum paid to the defendant as a preference. In holding the action would not lie, the Court said, (p. 154)

"The onerous duty of creditors which it is as-
"serted by the appellant (the Trustee) to inves-
"tigate when an offer of compromise is made to
"ascertain if the debtor can pay the amount of-
"fered and intends to pay it to all creditors alike,
"places too heavy a burden upon the creditors.
"When an offer of compromise is made the credi-
"tors are justified in believing that it is made in
"good faith to all creditors unless something oc
"curs to put them upon inquiry."

The most that can be said of the failure of a debtor to meet his obligations promptly is that it might raise a suspicion in the creditor's mind as to the debtor's financial standing. But even were this true this would not be sufficient to constitute reasonable cause. It is elementary that a mere suspicion on the creditor's part does not consti tute reasonable cause.

"Merely because some cause to suspect in-
"solvency of the debtor exists is not enough;
"there must be such a knowledge of facts as
"would induce a reasonable belief in the ordin-
"ary man that the debtor was intending to give
"a preference."

1 Remington on Bankruptcy, §1407.

Or as was said by Trieber, J., in Sparks v.

Marsh, 24 Am. Bank Rep. 280, 285, s. c 177 Fed. 739:

"The well settled rule of law is that mere "grounds of suspicion that a debtor is insolvent "or that a payment made by him is intended to "create a preference are insufficient to establish "the fact that a creditor who received it has rea "sonable cause to believe that a perference was "intended thereby. There must be substantial "evidence of reasonable grounds for such belief,"

In discussing this subject, Harrison, J., in Powell v. Gate City Bank, 24 Am. Bank Rep. 316, 326, s. c. 178 Fed. 609, said:

"Suspicion, fear and facts which arouse sus- "picion and fear that the debtor is insolvent and "intends to prefer a creditor, in the absence of "knowledge or notice of facts that give such a "creditor reasonable cause to believe the in "solvency of the intended preference are insuf- "ficient to avoid the latter."

In Tumlin v. Bryan, 165 Fed. 166, an action was brought by a Trustee in Bankruptcy of a partnership to recover payments made to a creditor as a preference. The District Judge rendered a decree in favor of the Trustee. On appeal it was held that the evidence was insufficient to sustain the decree and it was reversed. In delivering the opinion of the Circuit Court of Appeals, Shelby, C. J., said (pp. 168 and 169)

"A careful reading of the evidence does not "lead us to the conclusion that the defendant be-

"lieved the firm to be insolvent. But a belief "that a debtor is insolvent is a very different "thing from the belief referred to by the statute "—'reasonable cause to believe that it was in "tended' by the payments to give a perference. "It may often happen that one, though in fact "insolvent, will continue his business and make "payments in the usual way, without a thought "of preferring one creditor to another, and with "the hope and belief that he would finally be "able to pay all. If these payments were made "by the firm, without the thought of injuring "other creditors, and in the belief that it would "be able to pay them all, the defendant cannot "be charged with reasonable cause to believe "that a preference was intended. When a debtor "pays, and a creditor receives, the amount of a "just debt, the natural presumptions are in favor "of the good faith of the transaction. To let the "mere fact of the bankruptcy of the debtor with- "in four months make the transaction involved "voidable would be to create uncertainty and un- "easiness as to the probable result of every settle- "ment between debtor and creditor. Reasonable "cause to believe that a preference was intended "cannot be held to be proved by circumstances "that would merely excite suspicion. And cir- "cumstances may seem suspicious after the bank- "ruptcy occurs that would not appear unusual at "the time of their occurrence, and would then "have presented no 'reasonable cause' on which

"to found a belief of intended preference. Mer-
"chants and other business men constantly con-
"tinue to make payments up to the very eve of
"failure, and it would be disastrous to have them
"set aside on slight proof or mere suspicion."

These rules are firmly sustained by the authorities.

Ridge Ave. Bk. v. Sundheim, 16 Am. Bank Rep. 863, s. c. 145 Fed. 198.

Powell v. Gate City Bank, 178 Fed. 610.

Reber v. Shulman, 179 Fed. 574, aff'd 183 Fed. 564.

Grinstead v. Union Savs. & T. Co., 190 Fed. 546, 568.

Johnston v. Geo. D. Witt Shoe Co., 50 S. E. 153.

The leading case on the subject is the case of Grant v. National Bk, 97 U. S. 80. This case, it is true, was decided under the former law. It has, however, been cited, approved and followed in innumerable decisions under the present law and may easily be regarded as the foremost authority on the subject of what constitutes reasonable cause. In this case an action was brought by an assignee in bankruptcy to set aside a mortgage or deed of trust as a preference. It appeared that one Miller, the bankrupt, was indebted to the First National Bank of Monmouth, Ill., in the sum of $6,200.00, of which $4,000.00 consisted of a note which had been twice renewed and the balance was the amount which he had overdrawn

his account in the bank. Wanting some cash for immediate purpose, the bank advanced him $300.00 more on his giving them the deed of trust in question, which was made for $6,500,00 and was given to secure the indebtedness referred to. The question below was whether at the time of taking this security the officers of the bank had reasonable cause to believe that Miller was insolvent. The Circuit Court came to the conclusion that they had not and dismissed the bill. The Supreme Court on appeal affirmed the decree. Because of the importance of this case and also because of its strong application to the case under consideration, it is quoted at length. Bradley, J., in delivering the opinion said, (pp.81-83)

"It is not enough that a creditor has some "cause to suspect the insolvency of his debtor; "but he must have such a knowledge of facts as "to induce a reasonable belief of his debtor's in- "solvency, in order to invalidate a security taken "for his debt. To make mere suspicion a ground "of nullity in such a case would render the busi- "ness transactions of the community altogether "to insecure. It was never the intention of "framers of the Act to establish any such rule. A "man may have many grounds of suspicion that "his debtor is in failing circumstances, and yet "have no cause for a well grounded belief of the "fact. He may be unwilling to trust him further; "he may feel anxious about his claim, and have "a strong desire to secure it and yet such belief

"as the act requires may be wanting. Obtain-
"ing additional security, or receiving payment
"of a debt, under such circumstances is not pro-
"hibited by the law. Receiving payment is put
"in the same category in the section referred to,
"as receiving security. Hundreds of men con-
"stantly continue to make payments up to the
"very eve of their failure, which it would be very
"unjust and very disastrous to set aside. And
"yet this could be done in a large proportion of
"cases if mere grounds of suspicion of their
"solvency were sufficient for the purpose.

"The debtor is often buoyed up by the hope of
"being able to get through with his difficulties
"long after his case is in fact desperate; and his
"creditors, if they know anything of his em-
"barrassment, either participate in the same
"feeling, or at least are willing to think that
"there is a possibility of his succeeding. To
"overhaul and set aside all his transactions with
"his creditors, made under such circumstances,
"because there may exist some grounds of sus-
"picion of his inability to carry himself through,
"would make the bankrupt law an engine of op-
"pression and injustice. It would, in fact, have
"the effect of producing bankruptcy in many
"cases where it might otherwise be avoided.

"Hence the Act, very wisely, as we think, in-
"stead of making a payment or a security void
"for a mere suspicion of the debtor's insolvency,
"requires, for that purpose, that his creditor

"should have some reasonable cause to believe "him insolvent. He must have a knowledge of "some fact or facts calculated to produce such a "belief in the mind of an ordinarily intelligent "man.

"It is on this distinction that the present case "turns. It cannot be denied that the officers of "the bank had become distrustful of Miller's "ability to bring his affairs to a successful termi- "nation; and yet it is equally apparent, inde- "pendent of their sworn statements on the sub- "ject, that they supposed there was a possibility "of his doing so. After obtaining the security in "question, they still allowed him to check upon "them for considerable amounts in advance of "his deposits. They were alarmed; but they "were not without hope. They felt it necessary "to exact security for what he owed them, but "they still granted him temporary accommoda- "tions. Had they actually supposed him to be "insolvent, would they have done this?

"The circumstances calculated to excite their "suspicions are very ably and ingeniously "summed up in the brief of the appellant's coun- "sel; but we see nothing adduced therein which "is sufficient to establish anything more than "cause for suspicion. That Miller borrowed "money; that he had to renew his note; that he "overdrew his account; that he was addicted to "some incorrect habits; that he was somewhat "reckless in his manner of doing business; that

"he seemed pressed for money,—were all facts "well enough calculated to make the officers of "the bank cautious and distrustful; but it is not "shown that any facts had come to their knowl- "edge which were sufficient to lay any other "ground than that of mere suspicion. Miller had "for years been largely engaged in purchasing, "fattening and selling cattle. He had always "borrowed money largely to enable him to make "his purchases; for this purpose he had long been "in the habit of temporarily overdrawing his ac- "count; the note which he renewed was not a "regular business note, given in ordinary course, "but was made to effect a loan from the bank ap- "parently of a more permanent character than "are ordinary discounts; and his manner of doing "business was the same as it had always been. "That he was actually insolvent when the trust "deed was executed, there is little doubt but he "was largely indebted in Galesburg, in a different "county from that in which Monmouth is "situated; and there is no evidence that the of- "ficers of the bank had any knowledge of this in- "debtedness.

"Without going into the evidence in detail, it "seems to us that it only established the fact that "the officers of the bank had reason to be sus- "picious of the bankrupt's insolvency, when "their security was obtained; but that it falls "short of establishing that they had reasonable "cause to believe that he was insolvent."

The reasoning of this case applies directly here. To be sure this decision was under the former bankruptcy act. But as has been pointed out it has become the rule of decision as to what constitutes reasonable cause under the Act of 1898. Furthermore, the principles of construction laid down by the Courts in determining the force and effect to be given to the phrase "reasonable cause to believe" found in the former Act relating to preferences are equally applicable in considering the meaning of this phrase in the Act of 1898.

Stevenson v. Milliken-Tomlinson, 13 Am. Bank Rep. 201, s. c. 99 Me. 320.

The facts in this case fail utterly to show any grounds for charging the R. H. Herron Company with reasonable cause to believe a preference was intended by the payment and transfers attacked herein. There is only one circumstance disclosed by the record in any way tending to lead to that conclusion and that is that the Cleveland Oil Company was slow in its payments. This, however, as has been abundantly shown, is not enough to charge the creditor with knowledge of insolvency or having reasonable ground to believe a preference was intended. The record being destitute of any other evidence, the case of Grant v. National Bank applies with full force and it follows that the ruling of the referee that a preference existed is erroneous and must be reversed.

Particular consideration will now be given to the evidence for the purpose of substantiating this assertion.

THE EVIDENCE IN THIS CASE FAILS TO SHOW THAT THE R. H. HERRON COMPANY HAD REASONABLE CAUSE TO BELIEVE A PREFERENCE WAS INTENDED.

The Referee below reviewed the testimony at considerable length for the purpose of showing that the claimant here had reasonable cause to believe a preference was intended. With the greatest respect for the learned Referee, it is respectfully submitted that his conclusions are not supported by the record.

In the course of his opinion the Referee said: (Tr. p. 12)

"The bankrupt at the time of these payments "and transfers of its property not only knew that "it was insolvent, but it knew that it was so irre- "trievably so that it could not hope to continue "its business without some sort of reorganization "and its officers knew it could not make the pay- "ment which it did without disparity in its pay- "ments to its other creditors."

The evidence produced does not support this statement. There is nothing to show that at the time of the transactions attacked the bankrupt knew it was irretrievably insolvent. The only officer of the company who testified except Mr. Batchelder was Mr. Edson France. He was asked the question:

"Well, at the time you were having these con-
"versations with Mr. Sands, the company was in
"pretty bad shape financially, was it not?" (Tr. p. 37)

To this he answered, (Tr. p. 38) "I would not "consider it in very bad shape."

As he was the only officer who testified, except Mr. Batchelder who apparently had no knowledge on the subject at all, and as he said he did not consider the company in very bad shape, it is apparent that the statement as to knowledge of the officers is without support in the evidence.

The Referee refers to the fact that the claimant cut off the credit of the bankrupt. As will be shown by the authorities cited later, this fact does not show reasonable cause to believe a preference was intended. And taking this fact in connection with the record, there is not a line to show that the credit was curtailed because of a belief in the company's insolvency. Mr. Sands testifying as to this says, (Tr. p. 70)

"We considered at that time they were owing
"us quite a considerable sum and of course like
"other creditors, they reached the period where
"they should either increase or decrease. At that
"time we thought we had given them—that they
"were up to limit of their credit."

Asked further, "Isn't it a fact that you prac-
"tically cut off their credit on the last of
"August?" (Tr. p. 70) he said: (p. 70)

"It was not. They were privileged to call at

"our stores at Bakersfield, Taft and Maricopa "and buy supplies for emergency requirements "and if they wanted anything in excess of the "emergency requirement, they were to communi- "cate with the Los Angeles office."

Although a letter had been written as pointed out by the Referee limiting local purchases to $100, yet thousands of dollars worth of goods had been delivered after that. The claimant sold them in July something over $3,500.00 worth and in August $3,000.00 worth. The Referee seems to infer that the sales in August were because of a cash payment. (Tr. p. 14) The sales, however, amounted to $3,000.00 while the payment was only $1,500.00.

From the opinion of the Referee, it would seem as if the curtailing of the credit of the Cleveland Oil Company was something new in the dealings of the parties. The record shows, however, that this was customary in its dealings with this as well as other companies.

Sands testifies that early in the commencement of the business—on May 10th, 1909—he notified his manager at Bakersfield not to deliver over $100 worth on their own responsibility. (Tr. p. 113) Again on January 11, 1910, he limited their credit to $1,500.00. In relation to this he writes, (Tr. p. 130)

"They are owing us considerable money and "they have not acquired the habit of discounting "their bills which is our reason for their limited "credit."

On January 21, 1910, he limited deliveries to $1,000.00 for all three stores, feeling that was enough in view of the amount owed. (Tr. p. 132)

These acts bear out the testimony of Sands who said that the curtailing of credit was not due to the fact that he considered the company bankrupt or insolvent but was simply a business precaution and in accordance with their usual custom. (Tr. p. 113)

Sands testified that the average credit given to all oil companies was below $1,500.00. (Tr. p. 112) The indebtedness of the Cleveland Oil Company had arisen very much in excess of this and this was the reason for their precaution. At the time of the curtailing of their credit referred to by the Referee, he (Sands) regarded the company as prosperous as at any time in its existence and he considered it a prosperous oil company. (Tr. p. 73.)

This is substantially the testimony in relation to the curtailing the credit of the oil company. It shows clearly that none but the ordinary business relations existed between the parties. There was nothing unusual or suspicious about their dealings. The account of the debtor became larger than the creditor cared to carry and so it exercised the ordinary business precautions taken by careful business men under similar circumstances. At the time the creditor considered the debtor in as prosperous a condition as it ever was and there is no evidence or even a suggestion in

the record that the claimant here regarded the debtor as insolvent. And it is submitted that the Referee was not justified in his view that the curtailing of the credit showed reasonable cause on the part of the claimant to believe a preference was intended.

Continuing the Referee said that in the testimony of its manager and in the letters produced by it upon the hearing the claimant had furnished the evidence from which it must be found that when it received the payment made to it and the property returned to it, it was receiving a preference over the other creditors of the bankrupt. He first considers the return of the property to the claimant. Concerning this the Referee says. (p. 17):

"The proposition to return the goods came "from Mr. France and Mr. Sands agreed to it, "saying if he would take it back to the store, the "claimant would give credit on the account. The "only reason that was given for Mr. France offer- "ing to return the goods is that he told Mr. Sands "that they did not have any cash on hand at the "time and that they were willing to return the "casing. At that time the company owed a "great many other debts but a similar offer was "not made to any other creditors."

In this statement there is the insinuation that the claimant herein was attempting to overreach other creditors with the consent of the oil company. With the greatest respect for the learned

Referee, we say that he has not fully stated the facts and that his conclusions are not justified by the record.

In relation to the return of the property it may be said that the evidence shows that the transaction was in the ordinary course of business and in entire good faith.

It was quite common to take back property from companies and the claimant had done so frequently at a discount of twenty-five per cent from the price of new which was fair between both parties. (Tr. p. 107.) The return of the property here was due to a voluntary suggestion on the part of France, the president of the debtor company. Sands demanded money and there being none, France suggested that the property be returned and credited on the account. (Tr. p. 39.) He stated to Sands that his company had a string of pipe which it had in the field and was not using. (Tr. p. 44.) This was the pipe which was returned.

Sands testified in relation to the transaction that it was quite customary to take back second-hand material. (Tr. p. 85.) That the price at which they took it was more than a fair price. (Idem.) That France had told him that they had no use for the material and would be very glad if it could be received on account as a credit. (Tr. p. 86.) On the same occasion he told Sands that they had no money but were expecting some. (Tr. p. 86.) Sands further testified that he did not

know at any of the times when the property was returned that the debtor was insolvent and that he had no cause to believe a preference was intended. (Tr. p. 111.)

It thus appears that the transaction was an ordinary one—one such as frequently occurred in the usual course of business. The oil company was short of money. It had property it did not need so it returned it and was credited with it on the usual terms. There is nothing absolutely to show that the transaction was with a view to over-reaching the other creditors or with a knowledge of the debtor's insolvency. It was open and above board and in accordance with the usual custom of the creditor. There is no evidence to show that the claimant herein knew of the existence of any other creditors at the time. It is therefore respectfully urged that there was nothing in it to justify the view taken by the Referee.

As regards the payment of $2,000.00 on the 15th of September, 1910, France testifies that it was made in the usual course of business. (Tr. p. 45.) The Referee does not seem to question this transaction. But continuing, he says, (Tr. p. 18);

"Prior to this, however, facts had been "brought to the knowledge of the claimant that "were sufficient to have put a reasonably intelli- "gent man upon inquiry."

In support of this statement he gives the follow facts, (p. 18, Tr.):

"The general manager of the company knew

"as early as February 18, 1909, what were the "Cleveland Oil Company's holdings in the Kern "River field. He was advised by one of his dis- "trict managers on whose information he relied "that they were about to commence operations "upon ten acres in section 8-29-28, known as the "York Syndicate property, and also upon 17½ "acres in the same section known as the Vulcan "property and they were endeavoring to secure "other property. At that time the Vulcan had "one producing well and the York Syndicate two "wells. Mr. Sands had been by the property at "another time in the Kern River field and testi- "fies that they had quite a number of wells dug "there; that they seemed to be in a very prosper- "ous condition and they were all in where there "were producing oil wells, and in addition to that "at that particular time the company had a lease "on what was conisdered valuable oil land in the "Midway next to the Buick Oil Company. De- "cember 23, 1909, he knew from Dr. France, the "president of the company, that they had eight "producing wells and were getting from 8,000 to "10,000 barrels of oil perm onth."

It is respectfully submitted that there is absolutely nothing in these facts except what can be regarded as favorable to the claimant, and yet they are relied upon by the Referee as putting the claimant here upon inquiry.

The Referee then discusses the limiting of the credit of the oil company to $1,500.00 on January

11, 1910, and to $1,000.00 on January 21st, 1910. These facts have already been adverted to. They occured months before the transactions here attacked. The claimant in the meantime sold thousands of dollars worth of goods to the Oil company, thus showing by its own actions in the strongest way possible that it did not regard the Oil company as insolvent. They are significant in favor of the claimant as they show that the curtailing of the credit by the claimant later on was merely in the usual course of business.

The Referee then speaks of the four notes due respectively August 21, September 10, October 24 and November 16, 1910. On one of these notes the sum of $2,000.00 was paid. This payment was in the usual course of business. On another the sum of $2,823.37 was credited because of the return of the material that was not needed. The note of August 21 was not paid and the other note was not due at the time of the above transactions. These have been already referred to and considered and a further discussion of them is not necessary. The most serious inference that can be drawn from the fact that the notes were not paid when they were due is that the debtor was short of ready money but this, as will be abundantly shown, is very far from proving that the claimant had reasonable cause to believe the debtor insolvent. The Oil company was disappointed in not receiving money in time. (Tr. p. 22.) This is very ordinary and certainly does not show insolvency.

On August 22, 1910, Mr. Lyon, the secretary of the claimant, wrote to Sands a letter in relation to the shipment of casing to the Oil company. (Tr. pp. 139, 140.) The letter in itself is not of particular importance but on it Sands made the following indorsement in pencil: "Keep after them "at least twice a day. Make them come through." This memorandum apparently appealed to the Referee for commenting on it he says (Supp. Tr. p. 21):

"In common parlance, this, even for a credit "man, was 'going some' and after information "which caused him to give directions to keep "after a debtor at least twice a day and make it "come through, it could be hard to say that he "did not have reasonable notice to put him upon "inquiry."

This conclusion of the Referee, it is respectfully submitted is not justified by the language of the memorandum or anything done by the claimant in pursuance of it.

This was a mere memorandum addresed apparently by Sands to himself. He never communicated any such instructions to anyone. He never himself went after the Oil company twice a day nor did he instruct any one else to do so. He wrote several times afterwards to his manager. He did not tell him to go after the Oil company twice a day. Indeed he said nothing suggestive of any suspicion on his part that the Oil company was insolvent and he never expressed any doubt

of getting his money. On October 18, 1910, he wrote (Tr. p. 37):

"The Cleveland Oil Company owe us consider-
"able money and they are not in a position to sup-
"ply the ready cash. Their stock is almost worth-
"less from a stock market view, the last sales be-
"ing passed at 2¾ cents. They are endeavoring
"to arrange the company on a good financial
"basis but that will take some time," etc.

Here was no instruction to "keep after them "at least twice a day." In the letter there is no sugestion of doubt as to solvency of the company or that the company would not be able to meet its obligations or arrange its affairs. There is no doubt expressed but that the company would be able to arrange its affairs on a good financial basis. If Sands at the time he wrote questioned the ability of the company to arrange its affairs and felt it was necessary to "go after" them twice a day he would not have said "that "will take some time." He would have used some such expression as "but I do not believe it "can do so. Keep after them and make them "pay." To write "that will take some time" is equivalent to saying that the company will be able to arrange its affairs on a sound financial basis. The only question is as to the time it will take; there is none as to the ability to do so. There is no word in the letter to warrant the conclusion that Sands regarded the company as insolvent or

that there was any necessity of going after them twice a day.

The same general conclusions may be drawn as to the letter of August 29 (Supp. Tr. p. 39). In this letter to his district managers Sands says:

"This company has about all the credit we care "to extend them; in fact, we don't care to have it "increased over $50.00 between the various "stores."

Here is a mere curtailing of credit with no suggestion of insolvency, no doubt as to getting their money, no thought of it being necessary to go "after them at least twice a day."

These letters were both written after the memorandum above referred to. They show that Sands himself did not regard it as of any consequence or of enough importance to give a second thought to it.

Furthermore the very language of the memorandum is itself refutation of the inference placed upon it by the learned Referee. It reads "Keep "after them twice a day. **Make them come "through.**" The only conclusion that can be drawn from this language is that the Oil company could come through if they kept after it; that it had money and could pay its debts if required to do so. There is furthermore nothing in the memorandum to justify the position that it was necessary to go after them for fear the company was insolvent or for the purpose of overreaching the other creditors. There is no thought

in the memorandum that it was obligatory to go after them for fear there was not enough for all the creditors. It was apparently made without any serious thought, followed up with no word, deed or act and loses all meaning in view of the acts of Sands himself.

The learned Referee also says that the letters produced by the claimant showed that it had reasonable cause. (Tr. p. 18).

These letters are contained in the Transcript beginning with page 123 and in the Supplemental Transcript, pages 38-39. Some of them are referred to in the opinion of the Referee. To quote them would greatly protract the length of this brief. Concerning these letters, it may be said generally that there is not a line, word or syllable to show that the claimant ever suspected the insolvency of the Oil company or that its conduct at any time was with a view to over-reaching creditors or to secure a preference for itself. They all show the utmost good faith on the part of the claimant and they also show that it always had the greatest faith in the solvency of the Oil company.

The Trustee produced four witnesses: Batchelder, the secretary of the Oil company; Edson France, the president; W. C. Mushet, an expert, and John M. Sands, the treasurer of the claimant. Batchelder, the secretary, did not seem to be well informed about matters so his testimony may be disregarded. The testimony of the other three

witnesses is, however, signficant.

It is respectfully submitted that the testimony adduced by the Trustee herein fails to show that the appellant here had any reasonable cause to believe a preference was intended in the transactions here attacked. On the contrary, it shows the entire good faith of the appellant all through its dealings with the Cleveland Oil Company. This point will be made clear and the position of the appellant shown to be correct by a reference to the record itself.

Edson France was the president of the company. He was called as a witness by the Trustee and among other questions was asked if the company were not in pretty bad shape financially. To this he answered that he did not consider it to be so. (Tr. p. 38).

He further states that Sands—the representative of the appellant—never intimated that he knew the condition of the Cleveland Oil Company and never threatened to sue it. (Tr. p. 40). He told Sands when the latter demanded money that there was no money in the treasury and that was the reason they made no payment. (Tr. p. 41). But he said that they had oil in storage and that when they sold that and received the money they would make a payment. (Tr. p. 42). He further testified that the payment of $2,000.00 was made on the indebtedness of the company in the ordinary course of business. (Tr. p. 45).

Mushet, the expert accountant, appointed by a

committee of the stockholders to make an investigation of the books, made a report November 21, 1910. The report showed a liability to bondholders of $57,000.00 or $58,000.00. The bonded indebtedness was about $87,000.00. (Tr. p. 54). The book figures showed assets as follows: "Cash on hand, $129.26. * * * Oil properties and "leases. $253,163.05. * * * Devolpment in dif- "ferent companies, $172,852.36; the France-Mid- "way cook house, $1,521.51; office furniture and "fixtures, $770.92." (Tr. p. 57). "So that any "person who inspected the books on September "30, 1910, would find these apparent assets set "forth in the books" (Mushet's testimony, p. 57).

Sands, the manager of the R. H. Herron Company, was called as a witness by the Trustee in Bankruptcy.

He testified that he had not read articles in the paper published about the troubles of the Cleveland Oil Company. (Tr. pp. 65, 66). He never knew about Mushet's investigation or report until it became public. (Tr. pp. 66-114). He only knew about the arrest of the officers of the company by reading it in the public print. (Tr, p.68). He never made an investigation of the affairs of the company and it never furnished him a statement. (Tr. p. 68). He did, however, look at their property. His own language in this point is as follows (Tr. p. 72):

"Yes, I went by the property and they had "quite a number of wells dug there. I don't

"recollect how may. They seemed to be in a very "prosperous condition, they were all in where "there were producing oil wells, and in addition "to that, at this particular time, this company "had a lease on what was, and is, considered a "very valuable piece of oil territory as I under-"stand it in the Midway fields."

Continuing, he testified that while the company had a personal guaranty from Dr. France, it never went after him nor demanded the money of him. (Tr. pp. 81 and 82). The account was getting large and the bankrupt told Sands that they were expecting money soon. It was not long after that payments were made. There were payments pretty nearly every month. "It was quite "an active account." (Tr. pp. 84 and 85). He had no knowledge that Mushet was making an examination of the books and no knowledge that the stockholders were investigating the accounts. (Tr. pp. 86 and 87). He always thought it a good account and he had no reason to feel otherwise about it. (Tr. p. 87). To use his own language, "I never considered that there was any question "or doubt in regard to the account at all." (Tr. p. 87). He never questioned the account until the trouble with the postal authorties—the bankruptcy proceedings. (Tr. p. 87).

Further testifying he says that the notes which had been guaranteed by the R. H. Herron Company had been returned by the bank unpaid and that the bankrupt stated as a reason for not pay-

ing them that it had been disappointed in not receiving their money in time to protect them. (Tr. pp. 89, 90). It never gave any checks which were not good; it never gave any checks which it paid at a later date; and it never gave any checks with a request to hold them. (Tr. pp. 90 and 91). When asked why he did not make an investigation of the affairs of the Cleveland Oil Company when the notes were not paid, he said:

"These notes if you follow the records here "closely, I believe you will find each and every "note had a good and substantial payment there- "on, and that the account was active, it was not a "dead account. They were buying goods right "along." (Tr. p. 93).

Continuing, Sands says that he took no security for the notes as he considered that the company had security in the property and as an additonal safeguard it had Dr. France's guaranty. (Tr. p. 94). In this connection he says, (Tr. p. 94):

"Their property in the Kern River field was "according to conversations I had with Dr. "France, yielding good productions and I have "gone over the property that they had at the "Midway field and it had more than a prospective "valuation. It was adjoining the Buick Oil Com- "pany preporty which is one of the best proper- "ties, we understand, in the State. It joined "that."

Sands then testifies that in 1909 he obtained a

guarantee on a note for $5,055.00 for the reason that an extension had been asked on the note. On December 31st, 1909, a payment of $3,000.00 had been made on the note. (Tr. p. 96). He states he made no investigation of the affairs of the company when he received, the letter of October 1, 1910, from W. A. France stating that he would be no longer responsible for the debts because there was no necessity. (Tr. p. 97). He never tried to collect from France personally. (Tr. p. 98).

He further says that the circular as to the re-organization of the Cleveland Oil Company was sent out December 20th, 1910, and that he believed that the re-organization would be effected and that he had no reason to think the company was in a state of insolvency up to the time of the adjudication of insolvency February 20th, 1911. (Tr. pp 108, 109). He believed the company was solvent when the payment of $5,200.00 was made on the 15th day of September, 1910, and did not know it was insolvent. (Tr. pp. 110, 111). Nor did he know it was insolvent when he wrote the letter of October 26th, 1910, in relation to the return of the pipe that the company was insolvent. (Tr. p. 111). Nor did he know that the company was insolvent when the pumps were returned on November 25th, 1910. (Tr. p. 111).

Nor did he have any reasonable cause to believe the company insolvent at the time of the payment of the $2,000.000 on September 10th,

1910. (Tr. p. 111). He had no reasonable cause to believe a preference was intended at any of these times. (Tr. p. 112). He had no knowledge of the financial condition of the company up to the time that Mushet's report was published. (Tr. p. 112). He first saw Mushet's report December 20th, 1910. (Tr. p. 114).

The foregoing is the testimony of witnesses caled by the Trustee. We have reviewed it somewhat at length for the reason that the case depends upon whether the R. H. Herron Company had reasonable cause to believe a preference was intended when the payment of $2,000.00 and the transfers of property were made to it. The evidence as reviewed here shows that the R. H. Herron Company acted in entire good faith through the entire transaction. There is nothing to show it had reasonable cause to believe a preference was intended. When it is remembered that the law presumes the acts were regular and valid and that the burden of proof is on the Trustee, how far short the evidence falls becomes apparent.

The acts of the creditor bear out the statement that it acted in good faith and without any thought that the company was insolvent or that preferences were intended.

It appeared that the Cleveland Oil Company had been attached by the Associated Oil Company for $3,000.00. This information reached the R H. Herron Company October 16th, 1909. (Tr. p. 125). Yet after this as shown by the

records it sold the bankrupt a great many goods. (Tr. p. 113). This certainly would not indicate that the claimant here regarded the Cleveland Oil Company as insolvent.

Again although Sands had written a letter on July 22d, 1910, instructing the local managers not to deliver goods over the sum of $100.00, yet the claimant sold the company something over $3.500.00 in July, 1910, and nearly $3,000.000 in August, 1910. This conduct is entirely inconsistent with any belief in the company's insolvency. On the contrary it shows clearly that the claimant here regarded the company as sound. Creditors do not sell such large amounts to debtors they regard as insolvent.

Again, it is shown by the testimony here that the claimant never atempted to collect from the guarantor (France) the moneys due on the goods sold to the bankrupt. France, it seems had guaranteed the bills up to a certain date, yet although the bankrupt was behind in its payments, the claimant never made any attempt to collect the debts from him. This indicates that the R. H. Herron Company did not believe the Cleveland Oil Company was insolvent and bears out fully the statement of Sands that the account was a good one. Had the creditor here any doubts of the solvency of its debtor, it would have taken the steps usually taken by creditors under such circumstances and proceeded against the guarantor.

That under the circumstances as disclosed by the record here, no preference was created is abundantly supported by the authorities.

In In re Eggert, 3 Am. Bank Rep. 541, s. c. 98 Fed. 843, a debtor was behind in his payments to his creditor. The account was adjusted by giving the creditor an order on the City of Milwaukee for moneys to become due the debtor on a contract, the creditor allowing the debtor a discount of ten per cent. The creditor made no inquiries of the debtor to ascertain his solvency but he practiced no fraud or deceit and did not act in collusion with the creditor. It was held that there was no preference.

This case was affirmed on appeal in 4 Am. Bank Rep. 449, s. c. 102 Fed. 735. On appeal, Jenkins, J., after elaborate review of the authorities, said (p. 457);

"The facts established are within narrow com-
"pass. They are that Eggert was insolvent; that
"he had failed to meet his obligations promptly
"as they matured; that by the rules of the asso-
"ciation of which the Rundle-Spence Manufac-
"turing Company was a member, Eggert was not,
"while such debt remained unprovided for, en-
"titled to purchase goods upon credit, but only
"for cash; that the assignment of the claim
"against the city was not given or received by
"collusion of debtor and creditor. The finding
"is somewhat wanting. There is a failure to find
"that Eggert himself was conscious of his in-

"solvency. The aggregate of his assets and his "liabilities is not given. The only fact brought "home to the creditor and which it is claimed "should have aroused inquiry is that he was "somewhat behind in the prompt payment of his "obligations. We cannot say as a conclusion of "law, that knowledge of that fact standing alone "was sufficient to put the creditor upon inquiry. "Indeed, it may be said that a majority of mer- "chants absolutely solvent in the sense in which "the term is employed in the Bankrupt Act are "not at all times able to promptly meet their ob- "ligations as they mature. To hold that a credi- "tor receiving payment of or security for a past "due debt is, by the mere fact of knowledge that "the debt is past maturity, put upon inquiry of "his debtor's inability to pay all his debts, and "that under such circumstances he received pay- "ment or security at his peril would be to put at "hazard many business transactions and make "the act oppressive. The fact of such inability "coupled with other facts and circumstances "brought home to the creditor, might be sufficient "to put him on inquiry; but this is the only fact "from which the deduction is sought, that the "creditor had reasonable cause to believe his "debtor insolvent and standing alone it is insuf- "ficient to raise an inference of law that the "creditor is chargeable with knowledge of the "facts which inquiry would have elicited."

In In re Soudares Mfg. Co., 8 Am. Bank Rep.

45, a manufacturing corporation while a growing concern and actively engaged in its business within four months of its bankruptcy, obtained a present loan of money to pay off existing indebtedness, especially to meet advances made by another and to increase its output. It secured the loan by a chattel mortgage on its plant, the mortgagee relying upon an investigation alone of the title and apparent value of the machinery and fixtures and upon general statements on the part of the president of the corporation, but with no examination of the books of the corporation or other investigation of its financial standing and ability. The District Court held that the mortgagee had reasonable cause to believe a preference was intended. The decree, however, was reversed on appeal, by the Circuit Court of Appeals, the higher Court holding that the facts recited did not show reasonable cause.

In Hackney v. Raymond Bros. Clarke Co., 10 Am. Bank Rep. 213, it was held that an instruction that notice of facts sufficient to lead a man to the conclusion that a debtor "could not meet ob-"ligations as they matured in the ordinary course "of business" was notice of his insolvency was clearly erroneous.

In this case there was an absolute transfer of an account against the insolvent debtor in good faith to one who afterwards bought the latter's stock of goods and obtained credit for such account on the purchase price. There was no agree-

ment or understanding that such use was to be made thereof or that the purchaser of the account was to be protected by the creditor in any way. It was held there was no preference to the creditor to the extent of the money he received on the claim.

In Stevenson v. Milliken, 13 Am. Bank Rep. 201, s. c. 99 Me. 320, in an action by a trustee in bankruptcy to recover payments as preferences the defendants had no knowledge respecting the financial standing of the insolvent firm except that arising inferentially from a failure to make prompt payment of all their obligations. They were told by one of the partners that the firm was entirely solvent and that there was enough on the book accounts to care for all the other creditors. It was held that there was no preference.

In Turner v. Fisher, 13 Am. Bank Rep. 243, s. c. 133 Fed. 594, an action was brought to recover a preference by an insolvent to the defendant corporation. The agents of the defendant testified that they did not know of the insolvency of the debtor and that while the account from him was three months overdue, they were not pressing him and did not believe him to be insolvent. No fact was brought to their notice sufficient to excite in their minds as reasonable men a belief of the debtor's insolvency. It was held there was no preference.

In J. W. Butler Paper Co. v. Goembel, 16 Am. Bank Rep. 26, s. c. 143 Fed. 295, an attack was

made upon a mortgage given a creditor as a preference. The bankrupt had repeatedly stated to the representative of the creditor that trouble with his wife was the cause of his failure to pay his indebtedness; that he had a large interest in real estate held in her name; that his other indebtedness was not large; that when the real estate was sold, he could "square up with every "one." The creditor believed that the embarrassment of the debtor came from the cause stated, that the value of his property exceeded the amount of the debts and did not suspect indebtedness to other parties for considerable amounts. It was held that there was no preference. In delivering the opinion, the Court of Appeals said, (pp. 29 and 30):

"The good faith of these creditors in seeking "and accepting security for their account is not "impeached by the circumstances thus appear-"ing. Neither the fact that the accounts are past "due, nor the fact alone of financial embarrass-"ment under the conditions stated, establishes "the statutory ground for setting aside the se-"curity so received as an unlawful preference. "The bankrupt complains in his testimony that "the appellants (the creditors) refused to furnish "him supplies upon credit, after the security was "given and it is contended that such refusal is "evidence of their belief in his insolvency. It "appears, however, that they had required cash "payments for all supplies purchased during

"several prior months, so that no change of "policy is indicated. In any view the circum- "stance is of slight weight, as the extension of "credit to purchasers is governed by various con- "siderations; the solvent owner of property may "well be refused credit if known to be slow pay, "deceitful, litigeous or in litigation."

In Suffel v. McCartney Nat. Bank, 16 Am. Bank Rep. 259, it appeared that one Dickenson's business was selling musical instruments on terms, the business requiring considerable capital. He obtained loans from the bank giving the leases as collateral. In January, 1900, and in January, 1901, he gave statements to the bank showing a sound financial condition. In May, 1901, he gave notes to the bank for $1,200.00 with his father-in-law as joint maker, telling the cashier he wanted the money to pay off other indebtedness. On January 1, 1902, he gave an inventory of his stock to the bank and a statement of his liabilities as being $2,000.00 aside from what he owed the bank. This month his entire stock was destroyed by fire and a little later his household goods were destroyed. He had policies on both his stock and his furniture. About this time the cashier of the bank learned he owed other debts of at least two thousand dollars, that some of his small debts were being pressed for payment and that some of his checks were unpaid for want of funds. The cashier inquired of Dickenson whether he intended to resume business and was told that he

had about arranged with his creditors to pay them fifty per cent of the amount due them at once and they would give him time to pay the balance. The bank's claim was secured by notes on which the father-in-law of Dickenson was joint maker and was regarded as perfectly good. Nevertheless the cashier asked Dickenson to take up the notes with the insurance money, but did not insist in such payment. Dickenson, however, offered to make payment. It was held by the lower Court that the payment did not constitute a preference, the Court finding that neither the bank's cashier nor any of its officers believed Dickenson to be insolvent and that none of them had reasonable cause to believe that it was intended by said payment to give a preference. This judgment was affirmed on appeal. In delivering the opinion Cassaday, C. J., said, (p. 201):

"The Court found in effect that the facts "known to the cashier, at the time of such pay- "ment were such as would naturally produce in "the mind of a reasonably intelligent man a "doubt or suspicion of Dickenson's solvency, and "were such as would put a reasonably prudent "man on inquiry, if the bankrupt law required "the same diligence of creditors concerning pref- "erential payments that is required of grantees "in cases of fraudulent conveyances. The ob- "vious meaning of this language when construed "in conection with the other findings mentioned "is that the Court held as a matter of law that

"the present Bankrupt Act does not require the "same diligence of creditors concerning prefer- "tial payments that is required of grantees in "cases of fraudulent conveyances; and hence the "facts known to the cashier at the time of receiv- "ing the payment, though sufficient to produce in "his mind a doubt or suspicion of Dickenson's "solvency, yet they were insufficient to prove that "the cashier had at the time reasonable cause to "believe that Dickenson was then insolvent or "that in making such payment he intended to "give a perference to the defendant. This is in "harmony with the conclusion of the lengthy "opinion of the trial judge when he said in effect, "that the point to be decided was somewhat dif- "ficult but a considerable reflection had led him "to the conclusion that the knowledge of facts "and circumstances possessed by the cashier "were well calculated to produce a doubt or raise "a suspicion in the mind of an ordinary intelli- "gent man as to Dickenson's solvency, but not "such as was calculated to produce a belief of it; "and as that was essential to the plaintiff's "cause of action, he could not recover. Such find- "ings of fact seem to be sustained by the evi- "dence."

The Court then asks. "Are the conclusions of "the trial court in accordance with the law ap- "plicable to the case?" After a review of the authorities, the Court says, "We find no error" and affirmed the judgment.

In Matter of Alden, 16 Am. Bank Rep. 362, it was held that mere taking of security within the four month's period was not enough to charge the creditor with taking a preference. In this case Doyle, Referee, said (p. 379):

"Every person who receives security for a "debt has knowledge that he is being preferred "to the extent of being secured, but Sections 60a "and 60b require more knowledge than that. He "must know that the bankrupt is insolvent and "that by getting this security he will be enabled "to obtain a greater percentage of his debt than "any other creditor of the same class. Such "knowledge cannot be had unless he knows that "that the debtor is insolvent; that he has not "property enough to pay his general creditors; "and that by this security so given, he, the privi- "leged creditor, is being taken out of the class of "general creditors to be paid in full at their ex- "pense."

In Tomlinson v. Bank of Lexington, 16 Am. Bank Rep. 632, there was a mutual running account between a bank and one of its customers who for several years had been allowed to overdraw to meet current expenses upon the distinct understanding and agreement that the next succeeding deposit should be applied to existing overdrafts. It was held that deposits so made did not constitute preferences which must be surrendered before the bank could prove a claim upon the bankrupt's notes held by it even though

the deposits were made within the four month's period.

In this case Purnell, J., in delivering the opinion of the Court said, (p. 637):

"The bankrupt in the case at bar was strug-
"gling for existence—it was in financial straits,
"had made propositions of composition or settle-
"ment with its creditors and the bank in a legiti-
"mate way was extending a helping hand, agreed
"on a basis for extending credit, allowing over-
"drafts. There was a large amount, $13,100.00,
"due on notes endorsed by officers of the bank,
"which, if the manufacturing company could suc-
"ceed, the bank would realize from the assets of
"the bankrupt; if not the debt would be lost or
"at least much reduced. If such assistance on
"the part of banking institutions are to be con-
"demned, held to be preferences in case of bank-
"ruptcy many of the manufacturing and other
"institutions would suffer, especially in their
"early days of struggle, before they had attained
"a standing on a foundation strong enough to en-
"able them to resist the financial storm arising
"from an inability to sell their product or realize
"on accounts, bills of lading or other current
"assets. In short it would close them to all ave-
"nues of commerce and compel them to do a C. O.
"D. business on a very small scale, virtually
"putting them out of business as soon as it is
"proved they cannot meet their liability, are in-
"solvent as defined in the bankrupt act. Con-

"gress did not intend nor did it in fact ever enact "a law to effect this purpose."

In Hussey v. Richardson & Co., 17 Am. Bank Rep. 511, s. c. 148 Fed. 598, the facts were substantially as follows: The creditor had but recently been doing business with the bankrupt. It made inquiries usual among jobbers to determine whether he was entitled to credit and sold him about $2,000.00 worth of dry goods. He was slow in making payments as they matured, but with knowledge of that fact the mortgagee kept on selling him goods. Learning that the bankrupt had mortgaged his stock for $1,000.00, the creditor sent an attorney to the town where he was doing business to inquire. He learned the bankrupt had borrowed the $1,000.00 to pay a debt then due and was told the mortgage was executed with the approval of a wholesale grocery house which was one of his two remaining merchandise creditors. An investigation into his affairs followed. His stock was estimated by the attorney to be worth $5,000.00, although regarded by the bankrupt as worth $8,000.00. The indebtedness was represented as not being over $3,500.00. The bankrupt advised the attorney he could sell the stock for $6,000.00 and asked the attorney to stay over until the deal was closed. He told the attorney he was solvent, that his business was good and his assets more than sufficient to pay all his debts, but that he did not have enough capital to pay them promptly. The attorney concluded not

to wait until the sale was consummated, but before returning took a chattel mortgage to secure the debt. On an attack upon this mortgage as constituting a preference, it was held that the transaction was valid and not within the prohibition of the Bankruptcy Act.

Where a debtor, although in fact insolvent and while continuing to do his business in the usual way may make a payment to a creditor without a thought of the disparagement of the other creditors and with confidence in his ability to pay them all, the creditor receiving such payment in the belief that the debtor while paying him the debt in the common course of business, is acting without any purpose of giving him special favor, cannot be held to have had reasonable cause to believe that a preference was intended.

In re First Nat. Bank, 18 Am. Bank Rep. 766.

In Getts v. Jonesville, etc., Co., 21 Am. Bank Rep. 5, the facts showed that the creditor was undoubtedly suspicious and anxious to secure its claim. It knew that goods stated to be worth $4,000.00 in November, 1906, had been settled for by the insurers for $700.00 in April, 1907. It knew that the debtor's checks had been protested and that he was out of business and hard up. It was informed that there was some danger of the debtor's insolvency, although he was at that time a wage earner and apparently could not be made an involuntary bankrupt. On the other hand, it

relied on the debtor's property statement and trusted him within a month before receiving the payment by taking his signature as surety on a note for more than $600.00 and in reliance thereon delivered goods worth some $400.00. It was held that the facts failed to show a preference.

In Irish v. Citizens Trust Co., 21 Am. Bank Rep. 39, s. c. 163 Fed. 880, a bank received payment of notes from an insolvent corporation. It had demanded payment of the notes before. There was no doubt of the insolvency of the corporation at the time of the payment, but it did not appear that the insolvent intended a preference, as it hoped to be able to go on in business, and it did not appear that the bank had ever refused loans. It was held the facts did not constitute a preference.

In In re Wolf Co., 21 Am. Bank Rep. 73, s. c. 164 Fed 448, affirmed sub nom. Sharpe v. Allender, 22 Am. Bank Rep. 431, s. c. 170 Fed. 589, it appeared that within the four month's period, a bankrupt corporation in order to secure its note given for a loan to one who knew that it was in embarrassed circumstances, was pressing payment and threatening to sue, made an absolute assignment to the holder of the note, who in pressing payment was assured by those best calculated to know that the corporation's embarrassment was only temporary and that his debt was safe.

In holding that these facts did not charge the creditor with taking a preference, Archbold, D. J., said (p. 87):

"He (the creditor) may have known that the "report was unsatisfactory, as was evident be- "cause the re-organization was not carried out as "contemplated. But that is far from knowing "that it showed the company to be insolvent. Nor "did he manifest any more anxiety about his "claim than he had before that, as would have "been the case if he had such knowledge. The "idea that Allender (the creditor) could go to "the books is not to be thought of. Nor could he "expect to get access to the reports of the ex- "perts if it had been asked for. It is not intimate "and accessible information such as this, that a "creditor is bound by but that which is open to "observation and will yield to reasonable in- "quiry where it had not been expressly brought "home to him. No doubt in the present instance, "Allender was anxious over his debt and pressed "for its payment and may have expressed ap- "prehension with regard to it. But this is not to "be carried too far nor made to operate too "strongly against him particularly in view of the "assurance which he had received from those "best calculated to know on which he had a right "to rely, to the contrary."

If payments are made by a bankrupt firm to a creditor within the four month's period, without intent to injure other creditors and in the belief that it would be able to pay them all, the creditor cannot be charged with reasonable cause to believe that a preference was intended.

Tumlin v. Bryan, 21 Am. Bank Rep. 319, s. c. 165 Fed. 166.

In In re Neil, etc., Co., 22 Am. Bank Rep. 401, s. c. 170 Fed. 481, the creditor was doubtful of the debtor's financial standing and sent his agent to make inquiry. The agent's report was that the debtor was solvent, but was carrying too large a stock. Circumstances occurring to awaken the suspicion of the creditor, he went to where the debtor did business with a view to take legal proceedings and ask for the appointment of a receiver. He was assured by the debtor of his solvency and after consultations between the parties and their counsel, the debtor assigned to the creditor policies of insurance on property that had been destroyed by fire. It was held the assignment did not constitute a preference.

Where in an action by a trustee in bankruptcy in an action to recover chattels transferred by the bankrupt within the four month's period, the proof shows that the creditor received the chattels believing that the bankrupt while paying him his debt in the course of business, was acting without intent to favor him over other creditors, he cannot be held to have had reasonable cause to believe that a preference was intended.

Harder v. Clarke, 25 Am. Bank Rep. 756, s. c. 66 N. Y. Misc. 584.

Where a depositor in a bank accepted collateral for his deposit, the bank requesting him not to withdraw his deposit owing to the stringency in

the money market, but informing him that if a crisis came, he would be paid and it had sufficient assets, he is not chargeable with reasonable cause to believe a preference was intended, where he testified that he believed the statement of the bank and he had no thought or information of any kind that the bank was insolvent or anything of that kind.

Kimmerle v. Farr, 26 Am. Bank Rep, 818, s. c. 189 Fed. 295.

It is not enough that a creditor has some cause to suspect the insolvency of his debtor, but he must have such a knowledge of facts as to induce a reasonable belief of his debtor's insolvency.

Off v. Hakes, 154 Fed. 364.

In this case at the time of the giving of an alleged preference, the creditors agent was informed that in case of a sale of the bankrupt's goods at their then estimated worth, the bankrupt's ability to pay its creditors in full would depend on its ability to collect its then outstanding amounts of an undisclosed amount. It was held that such information was insufficient of itself to charge the creditor with knowledge that a preference was intended.

A leading case on the question is Stucky v. Masonic Sav. Bank, 108 U. S. 74. In this case an action was brought by an assignee in bankruptcy to have mortgages executed by the bankrupt to one Krieger declared void as a preference. In holding they were not preferences, the Court fol-

lowed the case of Grant v. National Bank, 97 U. S. 80, and quoted at length in a former part of this brief. Miller, J., in delivering the opinion said (p. 75):

"That case establishes the doctrine that a "creditor dealing with a debtor whom he may "suspect to be in failing circumstances, but of "which he has no sufficient evidence, may receive "payment or security without violating the bank- "rupt law. He may be unwilling to trust him "further; he may feel anxious about his claim and "and have a strong desire to secure it, yet such "belief as the act requires may be wanting. Ob- "taining additional security or receiving pay- "ment of a debt under such circumstances is not "prohibited by law.

"In the case before us the testimony of Krieger "himself as the one who best knows the strength "of the suspicion, if any, on which he acted, and "what evidence was before him must chiefly "control.

"We have examined his deposition very care- "fully. We think it bears the impress of candor "and it negatives the idea that he had reasonable "ground to believe Miller was insolvent, or that "he actually did believe it."

This reasoning applies directly here and would seem to be conclusive of the question under consideration.

Payments on a running account in the usual course of business by a person whose property

had actually become insufficient to pay his debts, where new sales succeeded payments and the net result was to increase his estate, and the seller had no knowledge or notice of the insolvency and no reason to believe an intention to prefer, are not preferences which must be surrendered as a condition to the allowance of proof of his claim.

Jaquith v. Alden, 189 U. S. 78, s. c. 9 Am. Bank Rep. 73.

A mortgage given on a manufacturing plant is not a preference where the mortgagee was unacquainted with the company and acted through an agent upon representations by the president and a report by the agent, although the company was in fact insolvent and although the mortgagee knew that a large part of the money borrowed was to be used in paying outstanding unsecured debts.

In re Soudan Mfg. Co., 113 Fed. 804.

In In re Oppenheimer, 140 Fed. 51, it was held that the fact that a bankrupt asked a creditor if he would accept merchandise from his store in part payment of his debt, does not charge the creditor, who accepted the offer, with reasonable cause to believe.

"At most," said Reed, J., in this case (p. 54), "this would only suggest that the bankrupt was "short of ready money and desired to make pay-"ments that way as far as he could instead of in "money."

The fact that a lender before advancing money

in accounts imposed onerous and oppressive terms does not show he had knowledge of the bankrupt's insolvency.

Van Iderstine v. Nat. Disc. Co., 174 Fed. 518.

In order that a trustee in bankruptcy may recover money paid as an alleged preference, there must be an advantage actually given to such creditor over others with knowledge on the part of such creditor of the intention of the debtor to prefer him and an intent and a guilty collusion on the part of a creditor with the debtor to accomplish this end.

Bacon v. Merchants Bank, 146 Ala. 521.

This case further held that the fact that the notes which the debtor paid bore interest at an usurious rate did not show reasonable cause.

The knowelge of a purchaser of a stock of goods from a partnership that the partners have personal liabilities and that the firm is indebted without knowledge that the partnership debts exceed its assets is not sufficient as a matter of law to charge the purchaser with knowledge of the intention to make a preference.

Lyon v. Clark, 129 Mich, 381.

The fact that one requested security for a loan that had run a number of years does not show reasonable cause.

Congleton v. Schreifhofer, 54 Atl. 144.

Nor does the fact that a bank demanded additional security for a loan.

Rankin v. Third Nat. Bank, 14 Nat. Bank. Reg. 4.

Nor does the fact that a debtor is compounding with his creditors.

Wilson v. Weigle, 62 Atl. 458 (N.J.)

Nor is the fact that a creditor suspected the debtor to be in an embarrassed condition and was anxious about his debt when he received a partial payment.

Burnham v. Ft. Dodge, etc., Co., 123 N. W. 230.

Nor the fact that he fails to meet his obligations promptly.

Arkansas Nat. Bank v. Sparks, 103 S. W. 626 (Ark.)

Nor the refusal by a bank longer to discount the notes of a customer and the taking of a judgment note.

Keith v. Gettysburg Nat. Bank, 10 Am. Bank Rep. 762.

The fact that bankers enter into an agreement with a depositor to borrow his deposit, giving him security, does not charge the depositor with having received a preference.

Harmon v. Feldheim, 91 N. W. 744 (Mich.)

And generally it may be said that the authorities fully support the doctrines that reasonable cause is not shown by the fact that the creditor knows his debtor is in an embarrassed condition financially; that the debtor is slow and uncertain

about meeting his obligations; and that the creditor is anxious about his debt; or takes security for it; or is importunate in requiring payment, where there is nothing to show that the creditor has knowledge of facts charging him with notice of the debtor's insolvency—that is, that his assets are not equal to his liabilities.

Curtiss v. Kingman, 20 Am. Bank Rep. 95, s. c. 159 Fed. 880.

In re Peacock, 24 Am. Bank Rep. 159.

In re Evans Lumber Co., 23 Am. Bank Rep. 881, s. c. 176 Fed. 643.

Sparks v. Marsh, 24 Am. Bank Rep. 280, s. c. 177 Fed. 739.

Powell v. Gate City Bank, 24 Am. Bank Rep. 316, s. c. 178 Fed. 609.

Hamilton Nat. Bk. v. Balcomb, 24 Am. Bank Rep. 338, s. c. 177 Fed. 155.

In re Houghton Web Co., 26 Am. Bank Rep. 202.

In re Varley, etc., Co., 26 Am. Bank Rep. 840, s. c. 191 Fed, 459.

Chic, etc., Co. v. Roebling Sons Co., 107 Fed. 71.

In re Pettingill, 135 Fed. 218, s. c. aff'd 14 Am. Bank Rep. 757.

Debus v. Yates, 193 Fed. 427.

Edwards v. Corondelet Mill Co., 108 Mo. App. 275.

Guichtel v. First Nat. Bank, 66 N. J. Eq. 88.

Stackhouse v. Holden, 66 N. Y. App. Div. 423.

Sierine v. Stover, etc., Co., 64 S. C. 457.

Stratton v. Lawson, 27 Wash. 310.

Dunlap v. Thomas, 28 Wash. 521.

In re Wright, 2 Nat. Bank Reg, 490.

Johnston v. Witt Shoes Co., 50 S. E. 153.

Coder v. Arts, 152 Fed. 943.

The principle governing in the foregoing authorities applies directly here and leaves no doubt of the soundness of the conclusion that as a matter of law the Trustee here has failed utterly to discharge the burden of proof imposed upon him and that he has failed entirely to show that the R. H. Herron Company was guilty of receiving preferences in the transactions here sought to be set aside. Under the unquestioned rules of law as shown by the citations herin given there must be a clear showing by the Trustee of facts which will charge the creditor with notice so as to bind him with reasonable cause. We have analyzed at some length the testimony and it is respectfully submitted that there is a dearth of any evidence to show that any of the requirements of the law have been complied with by the Trustee, but that on the contrary every act of the creditor here was characterized by entire good faith and was wholly free from even an insinuation of unfairness or over-reaching.

The learned Referee says that notice of facts that would invite a man of ordinary prudence to

inquiry under similar circumstances is notice of all the facts which a reasonably diligent inquiry would disclose. This is an elementary and well settled rule which no one will deny. With the greatest respect for the learned Referee it is submitted, however, that there is no room for the application of this rule here. But while appellant strenuously denies that the facts here were such as to put it on inquiry, if it be supposed for the sake of the argument, they did put the claimant here on inquiry, what would an inquiry here have shown?

The case here must be judged by the record. It cannot be assumed for the purpose of overthrowing this claim that the Oil company was known to be insolvent or that such was its general reputation in the community.

Suppose the claimant had inquired of the president. This, as far as the record goes, would show nothing that was not favorable because the president testified that he did not consider the company in bad shape financially. (Tr. p. 38.)

Suppose the claimant had made an examination of the books of the company. This would not have disclosed that it was insolvent. It seems that the stockholders appointed an expert—one Mushet—to examine the books that they might ascertain the condition of the company's affairs. It may be remarked, in passing, that if the stockholders had to hire an expert to learn the standing and condition of the company, the claimant

could hardly be charged with notice of that standing and condition. But what did the books show, according to the report of the expert? The book figures showed assets and liabilities as follows:

"Cash on hand, $129.26. * * * Oil properties "and leases, $253,163.05. * * * Development in "different companies, $172,852.55; the France-"Midway cook house, $1,521.51; office furniture "and fixtures, $770.92." (Tr. p. 57.)

The liabilities, acording to the same report, were as follows, (Tr. p. 54):

"The liabilities outside of the liability to stock-"holders and bondholders was in the neighbor-"hood of $57,000 or $58,000. * * * The bond issue "was $100,000 and there seemed to be $13,000 un-"issued which would make about $87,000 "issued."

According to the expert, "Any one who in-"spected the books on September 30, 1910, would "find these apparent assets on the books." (Tr. p. 57.)

The conclusion is irresistible that an examination of the books would show the company to be solvent.

There is no evidence in the record as to the general reputation of the company in the community, no evidence that it was at all heavily indebted, no evidence that it was being harrassed or pursued by creditors; no evidence that its credit was not good. There is an utter dearth of

testimony in the record to show that if the claimant here had made inquiry, that the inquiry would have led to any knowledge. The Trustee here has failed to produce anything that would charge the claimant with knowledge had it made the inquiry trustee claims it was called upon to make. Therefore, he has not sustained the burden of proof imposed upon him by the law.

The company all this time had very valuable leases. It is true that later these went back. But this appeal is to be determined by what appeared at the time and not by what occurred subsequently. The claimant relied upon these leases as well as upon other things as it was justified in doing.

It is respectfully submitted that even if the claimant here was put on notice and bound to make inquiry—which we insist on the facts of this case was not necessary—nevertheless there is nothing in this record that would disclose to the claimant herein that the Oil company at the times of the transactions here attacked was insolvent, that is that the aggregate of its property at a fair valuation would not be sufficient in amount to pay its debts.

CONCLUSION

With the greatest respect for the learned Referee, it is suggested that he confused the facts which existed at the time of the transactions involved with facts that happened subsequently. In this an injustice—of course unwittingly—

has been done to the appellant. Subsequent events often prove persons to be insolvent who at the time, were apparently perfectly solvent and amply able to pay their debts. This shows the danger of considering anything arising subsequently in determining the question of reasonable cause.

In this case there was no evidence whatever to the effect that the bankrupt here intended to favor the claimant here as against the other creditors. There is nothing to show that it intended a preference. There is no showing of any collusion or understanding between the parties by which the claimant was to profit at the expense of the other creditors. The Referee was compelled to rely upon a presumption to establish the intent of the debtor. It does not appear that the claimant was aware of any other indebtedness of the bankrupt or that it had other creditors threatening its solvency. There is nothing to show that the claimant believed or had reason to believe the debts exceeded the assets. There is no evidence that the claimant knew it was being paid at the cost of the other creditors. There is no evidence that the claimant knew of the insolvency of the debtor or suspected it. While anxious about its claim it was no more so than it had been all through its dealings with the bankrupt. That it did not suspect bankruptcy is best shown by its own acts for but a short time before the acts attacked here, it had trusted the bankrupt with thousands of dollars worth of goods.

As the relations of the parties had been the same from the beginning, this would certainly show the claimant did not suspect insolvency. All that the evidence proves is that the company was embarrassed for ready money. It had valuable properties worth far more—according to the report of the expert— than all its debts including its bonded indebtedness. It was hopeful and expected to succeed up to the very end, but it had difficulty in meeting its obligations promptly. This is the case of thousands of others who bring their enterprises to successful conclusions. The law encourages those who are struggling to extricate themselves from their financial difficulties. The law looks with leniency on those who deal with them in good faith under such circumstances. It is respectfully submitted that the rule laid down by the Referee is not in keeping with the broad view adopted by the Courts and that the order confirming the report of the Referee should be reversed.

Respectfully submitted,

GEO. E. WHITAKER,

Attorney for Appellant and Claimant.

No. 2254

IN THE

United States

Circuit Court of Appeals

FOR THE NINTH CIRCUIT.

R. H. Herron Company, a corporation,
Appellant,

vs.

William H. Moore, Jr., Trustee in Bankruptcy of the Cleveland Oil Company, a corporation,
Appellee.

Brief of Respondent William H. Moore, Jr., Trustee of the Estate of the Cleveland Oil Company, a Corporation, Bankrupt.

STATEMENT.

The facts of this case have been stated in full in the opinion rendered by the referee in bankruptcy on the 14th day of October, 1912 [Tr. p. 4 to 8, inclusive], and in the brief of appellant on file herein. Respondent therefore deems it unnecessary to recite at length all the facts involved in this case.

The issues involved herein have been thoroughly considered by the referee in bankruptcy and in the United States District Court of the Southern District of California, Judge Wellborn sitting, wherein Judge Wellborn affirmed the decision of the referee. The facts are briefly as follows:

On the 12th day of January, 1911, an involuntary petition in bankruptcy was filed against the Cleveland Oil Company, and thereafter, on the 20th day of February, 1911, the Cleveland Oil Company was duly adjudicated a bankrupt. After said adjudication the appellant, R. H. Herron Company, filed a claim against the bankrupt estate for the sum of $14,804.32. Thereafter the trustee of said bankrupt estate filed an objection to said claim on the ground that on the 15th day of September, 1910, the bankrupt had paid to R. H. Herron Company the sum of $2000.00 which constituted a preference, and that on October 31, 1910, the bankrupt returned to the Cleveland Oil Company oil well casings of the value of $2823.37, and that said payment constituted a preference, and that on the 31st day of December, 1910, the bankrupt returned to the company two pumps of the value of $300.00, which payment constituted a preference. Said claim and the objection thereto came regularly for hearing before the referee in bankruptcy, and after hearing all the evidence concerning the same, and having considered the issues involved, the referee found that each of said payments constituted a preference, and held that the claim of the company in the sum of $14,804.32 be not allowed unless it surrender to the trustee said preferences, together with interest thereon from the time of payment.

The claimant filed a petition for review in the United States District Court of the Southern District of California, and on said review the Honorable Olin Wellborn, district judge, after fully considering the evidence and the issues involved, confirmed the findings and decision of the referee.

THE PAYMENTS SET OUT IN THE OBJECTION TO APPELLANT'S CLAIM WERE VOIDABLE PREFERENCES, AND ALL OF THE ELEMENTS NECESSARY TO CONSTITUTE SAID PREFERENCES WERE SUPPORTED BY THE EVIDENCE.

It was necessary for the trustee in this case, in order to support his objections to the proof of debt by the claimant in that said claimant's claim should be disallowed for the reason that it had received certain preferences, to show:

First: That said payments were made within four months preceding the filing of the petition in bankruptcy and that they were made on a pre-existing debt owing to the claimant.

Second: That at the time said payments were made to the claimant said bankrupt was insolvent.

Third: That said bankrupt in making said payments intended to give to the claimant a preference.

Fourth: That the result of said payments was to enable the claimant to obtain a greater percentage of his debt than other creditors of the same class.

Fifth: That at the time said payments were made the claimant had reasonable cause to believe that it was intended thereby to give it a preference.

Evidence was introduced by the trustee supporting each of the above elements of a preference, and the ref-

eree in bankruptcy and the United States District Court on review from the hearing before the referee, found that each of said payments constituted a preference, and that the claim should be disallowed unless said preferences were paid over to the trustee.

At the time the first payment in controversy was made to the claimant, the bankrupt was indebted to the claimant in approximately the sum of $20,000.00 for goods, wares and merchandise sold to said bankrupt by the claimant, part of which was carried in open account against the bankrupt, and the balance thereof was represented by certain notes executed by the bankrupt in favor of claimant. [Tr. pp. 119-120.]

The payments in controversy were made on the 15th day of September, 1910, the 31st day of October, 1910, and the 31st day of December, 1910, all of which were made within four months preceding the filing of the petition in bankruptcy, which was filed January 12, 1911.

The findings of the referee and the decision of the District Court to the effect that at the time these payments were made the bankrupt was insolvent, is sufficiently supported by the evidence. The schedule in bankruptcy shows that the bankrupt was indebted in secured claims in the sum of $103,211.02 and in unsecured claims in the sum of $34,234.61. [Supp. Tr. pp. 10 to 28, inc.]

The property which came to the hands of the trustee in bankruptcy, being property held by the bankrupt at the time of the filing of its petition, did not exceed the sum of $10,000.00. [Tr. pp. 49-51.]

Mr. Edson France, treasurer and vice-president, testified that between the 12th day of September, 1910, and the 6th day of March, 1911, there was no material changes in the assets or liabilities of the company. [Tr. p. 26.]

Mr. W. J. Batchelder, one of the directors of the bankrupt and secretary of the company, testified that he was familiar with the assets and liabilities of the company, and that there was no particular change in the assets of the company between the 12th day of September and the date of the bankruptcy. [Tr. p. 116.]

Mr. W. P. Mushet, an expert accountant, on the 26th day of October, 1910, made an examination of the books, accounts and the affairs of the corporation, and made a report thereon on the 21st day of November, 1910. The report shows that on September 30, 1910, the bankrupt's liabilities amounted to $57,529.06 and in addition thereto a bonded indebtedness of $100,000.00; and that its assets consisted of leases known as the California Kern, France Mid-Way, Vulcan Lease, and York Syndicate, and the office furniture and fixtures, which cost $770.92. [Tr. pp. 54, 55, 56, 57.]

The leases held by the company were of very doubtful value and were forfeited to the lessors. [Testimony of Wm. H. Moore, trustee, pp. 50, 51, 52, 53.]

It can hardly be contended that these assets out of which the trustee did not realize in excess of $10,000.00 were at any time during the four months of sufficient value to pay the unsecured indebtedness of the company, amounting to over $57,000.00.

At the time each of the payments was made, the bankrupt being insolvent, it must be held that the bankrupt intended to give a preference to the claimant. The intent in the absence of other proof may be shown by its equivalent in law. Proof of the inevitable result of the transaction, which in this case was to give a preference and to create an unequal distribution of the bankrupt's estate. At the time the payments were made the bankrupt, by the testimony of its officers, Edson France and W. J. Batchelder, not only knew that it was insolvent, but knew that it was irretrievably so; and that it could not make the payments which it did without disparity in payments to its other creditors.

If the effect was to create a preference and such was its natural consequence, it must have presumed to have intended that which was the necessary result of his act.

In re Dorr, 196 Fed. 292;
Western Timber Co. v. Brown, 196 U. S. 502, at 508, 25 Sup. Ct. 339, 49 L. Ed. 571;
Remington on Bankruptcy, Vol. III, page 417.

In view of the large unsecured indebtedness to other creditors existing at the time these payments were made, and in view of the small amount of assets owned by the bankrupt at the time, it is evident that the payments enabled the claimant to obtain a greater percentage of its debts than other creditors of the same class.

The remaining element of preference as to whether or not the claimant at the time of receiving each of said payments had reasonable cause to believe that it was intended thereby to give it a preference, is the only

issue which was vigorously contested by the claimant in this proceeding.

The trustee was at great disadvantage in this case for the reason that the parties interested and the witnesses were very reluctant and unwilling to give the court the information which they possessed.

Mr. Sands for the reason that he was one of the officers of the claimant, and very desirous that his company's claim should be allowed.

Mr. France and Mr. Batchelder for the reason that at the time the testimony was given they were under arrest by the United States postal authorities on account of transactions connected with the Cleveland Oil Company.

Thus the trustee was unable to present to the court a full and complete statement of the transactions surrounding these payments, and the transactions between the claimant and the bankrupt, but the evidence that he succeeded in obtaining and putting before the court was sufficient to convince the court that at the time each of the payments were made claimant, it had reasonable cause to believe that a preference was intended.

The evidence shows that as early as January 11, 1910, the claimant had commenced to be suspicious of the ability of the bankrupt to pay for the goods sold to it, and on that day it notified the Oil Well Supply Company at Taft, California, that it was privileged to deliver to the Cleveland Oil Company supplies to the amount of $1500.00, but nothing in excess of that amount without communicating with the Los Angeles office. And in that letter the treasurer said:

"They are owing us considerable money, and they have not acquired the habit of discounting their bills, which is our reason for the limited credit." [Tr. p. 130.]

On January 21, 1910, the treasurer notified the Oil Well Supply Company at Bakersfield that the amount of the open account of the Cleveland Oil Company was $4819.50, and they owed a note due February 28th for $2055.42, and one due February 15th for $6617.16, and that they felt this was quite enough, providing the information which was given them by their district manager at Bakersfield, the other day, was correct. That they were owing considerable sums for other bills, and there were other creditors who were not able to get their money. This letter also required a report from each of the representatives of the company in his district, and permitted them to make deliveries amounting to $1,000.00 for all three stores. [Tr. p. 132.]

From that time on there was more or less correspondence between the claimant and the stores concerning the amount of credit which was to be given to the bankrupt, and commenting upon the trouble of obtaining payments from bankrupt. At the last of August the credit of the bankrupt was practically suspended, and from that time on the total amount of the sales of the claimant to the bankrupt did not exceed the sum of $100.00, whereas prior to that time the sales had amounted to thousands of dollars.

Mr. Sands, the credit man, gave as an explanation of this that the account of the bankrupt was becoming too large, and was larger than the amount of credit usually given to oil companies by his concern, but it

does not appear from the letters in evidence that this was the case. The claimant did not seem to be concerned as much over the amount of the indebtedness owing to it as it did over the fact that it could not obtain any payments on account from said bankrupt. On the 21st day of September, 1910, the claimant notified several stores at Bakersfield, Taft and Maricopa, in Kern county, that the bankrupt was only privileged to buy supplies for emergency requirements not to exceed $50.00 in any one order, and that if the bankrupt required anything in excess of that amount that it was to be communicated to the Los Angeles office, where the claimant maintained a credit man. Prior to that, on July 22, the managers of the stores were advised that the state of the account of the Cleveland Oil Company was such that they were only to deliver goods to the Cleveland Oil Company in small quantities not to exceed $100.00, and anything in excess of that amount was to be referred to the Los Angeles office.

On August 6th the claimant authorized its agents to deliver to the bankrupt 11,000 feet of #28 casing, stating that the reason therefor was that the bankrupt had promised to pay its equivalent in cash. [Tr. p. 136.]

On the 22nd day of August, 1910, the claimant was advised that the refinery of the Warren Brothers, which was operated for the benefit of the Cleveland Oil Company, was destroyed by fire, and the secretary of the claimant wrote to Mr. Sands as follows:

"Had a talk with Mr. Batchelder of the Cleveland Oil Company this morning. It seems that their refinery in the Kern River field burned down Saturday

and they are having trouble in raising the $1700.00 necessary for the 1000 feet of 8" casing for the Kern River field. It seems that the National sent them a car of 8¼" to the Midway field, and by mistake their superintendent unloaded it and hauled it out. You know we gave them 1000 feet there and the result is that they have 2000 feet too much in the Midway field, and have none in the Kern River field. They have not taken care of their note due today. We are simply giving you this information that you may be in touch with the matter."

Mr. Sands endorsed on this letter a most singular notation, to-wit:

"Keep after them at least twice a day. Make them come through."

Although Mr. Sands reiterated time and time again in his testimony that he felt that this account was perfectly safe and that the Cleveland Oil Company had sufficient assets to pay all of its debts, he must at that time have had some reasonable notice to have put him on inquiry as to their true condition, for such a statement would hardly come from a credit man who felt assured that his firm's account was perfectly good.

Mr. Sands, the credit man of the claimant, testified that he did not at any time make an investigation of the financial condition of the bankrupt, but we are of the opinion that he was at the time these payments were made, acquainted with the true condition of the company, for on the 18th day of October, 1910, he wrote to his district manager at Taft as follows:

"'The Cleveland Oil Company owes us considerable money and they are not in position to supply the ready cash. Their stock is almost worthless from a stock market view, the last sale being passed at two and three-fourths cents. They are endeavoring to arrange

the company on a good financial basis, but that will take some time. They have arranged to deliver us a string of ten #40 casing on the well they are drilling in the Midlands, and we have promised to give them credit when delivered to our stock at Moron at list less 25%."

The statements in this letter to the effect that "they are endeavoring to arrange the company on a good financial basis, but that will take some time," and the statement that "their stock is almost worthless," would certainly lead to the conclusion that Mr. Sands had considerable information regarding the financial condition of the Cleveland Oil Company previous to the time that letter was written.

The claimant during the last part of August and the first part of September was pressing the Cleveland Oil Company for payment of account, and being unable to obtain the same Mr. Sands informed Edson France that he was going to try to collect the account from his brother, W. A. France, who had personally guaranteed the account of the Cleveland Oil Company. It was during this conversation with Mr. Sands that Edson France informed Mr. Sands that the company did not have any money in the treasury at the time, and that the production had not brought in enough to pay him or the pay roll and other expenses. [Tr. p. 41.] Just prior to the time of the payment made on September 31, 1910, Mr. Sands called at the office of the claimant to explain to the claimant why the Cleveland Oil Company did not pay some of the money that it had demanded. [Tr. p. 37.] At that time Mr. France informed Mr. Sands that the company did not have any

money. [Tr. p. 37, Tr. p. 30.] And that the company could not make a payment on account [Tr. p. 31], and he told him that they had some pipe in the oil fields which he would turn over to him if he would take the same [Tr. p. 37], and he further stated to Mr. Sands that they would have to take the casing, as the company did not have any cash on hand. [Tr. p. 32.] Mr. Sands agreed to accept the casing and gave the company credit for the same less 25% of the cost thereof. As the result thereof sufficient casing was returned to claimant to entitle the bankrupt to a credit of $2000.00 under the agreement. At this time other creditors were after their money, but the bankrupt did not make a similar offer to them. [Tr. p. 39.]

At the time the $2000.00 cash payment was made the bankrupt had been promising the claimant cash for several weeks. The notes of the claimant on which said $2000.00 was credited had been endorsed and discounted by the claimant at its bank. They were not paid when due, and claimant had to take up the notes at the bank, and they were advised that the Cleveland Oil Company did not have the money at that time to protect the note.

Claimant's contention that on the 31st day of December, 1910, when the pumps were returned to it by the bankrupt, that it did not have any knowledge which would lead them to suspect that the Cleveland Oil Company was insolvent or that they were receiving a preference over other creditors, or that they did not have knowledge of any facts which would put an ordinary prudent man upon inquiry as to the real condition of said Cleveland Oil Company, is wholly without merit.

For prior to the 31st day of December, 1910, in addition to the information mentioned above, the claimant had among its files in its credit department certain clippings from Los Angeles newspapers which recited the fact that the Cleveland Oil Company was in a bad way financially, and that its officers were under arrest by the United States postal authorities on account of fraudulent transactions connected with the company. [Supp. Tr. p. 35.]

It is probably true that the claimant, being satisfied with the guarantee which it had received from W. A. France, the president of the company, and who they believed to be financially responsible, was not as diligent in investigating the affairs of the company as they otherwise would have been, but this certainly could not relieve them from the duty of making a reasonably diligent inquiry, which, if made, would have disclosed to them that at the time the payments were made the Cleveland Oil Company was insolvent, and that by receiving said payments they were receiving a preference over other creditors. The referee in bankruptcy and the learned district judge were satisfied that the facts disclosed by the evidence were such as to have put a person of ordinary business intelligence on inquiry, and to induce the belief that it was given more than other similar creditors.

It is not necessary that the claimant should have had knowledge that a preference was intended, nor was it necessary that the claimant should believe that a preference was intended. It was only necessary that the claimant should have had a reasonable cause to believe that a preference was intended, which is far different.

The doctrine as laid down by the federal courts in construing this element of preference is that notice of any facts that would incite a man of ordinary prudence to inquiry under similar circumstances is proof of all the facts which a reasonably diligent inquiry would disclose.

In re Eggert, 102 Fed. 735;

Stuart v. Farmers-Merchants Bank of Cuba City (Wis.), 21 Am. B. R. 403;

Grant v. Bank, 97 U. S. 80;

Bank v. Cooke, 95 U. S. 343;

McElvian v. Hardesty, 22 Am. B. R. 320, 169 Fed. 31;

Wright v. Sampter, 18 Am. B. R. 355, 152 Fed. 196;

Wright v. Skinner Manufacturing Co., 20 Am. B. R. 527, 162 Fed. 315;

In re Goodhile, 130 Fed. 471;

Sundheim v. Ridge Avenue Bank, 15 Am. B. R. 132;

In re Virginia Hardwood Mfg. Co., 15 Am. B. R. 135;

In re Dorr, 196 Fed. 292;

Collier on Bankruptcy, 9th Ed. 815, and cases cited;

Coder v. McPherson, 18 Am. B. R. 523, 152 Fed. 951;

Huttig Mfg. Co. v. Edwards, 20 Am. B. R. 349, 160 Fed. 619;

Rogers v. Fidelity Savings Bank & Loan Company, 23 Am. B. R. 1, 172 Fed. 735;

In re Harrison Bros., 202 Fed. 243.

In re Dutschle, 25 Am. B. R. 348, 182 Fed. 435, it appeared that within four months prior to the bankruptcy payments had been made on notes for a lumber account which had frequently gone to protest and had been the subject of constant complaint. Notwithstanding this fact, the claimants had an order for more lumber and were about to fill it when they learned that the bankrupts were in difficulty, and did not do so. They were also advised on inquiry at the bank where the bankrupts were in business that their condition had improved and it was thought that they would pull through. It was held that the facts in this case concerning the critical embarrassment of the bankrupts were sufficient to have put the claimants on inquiry, and that their claim for a balance due on the notes could not be allowed unless they surrendered the payments received during the four months' period which constituted voidable preferences.

In re Dorr, 196 Fed. 292, C. C. A. 9th Circuit, decided by this court May 6, 1912, it was held that the fact that the bankrupt gave to the claimant a check for $26,000, telling him that there was no funds in the bank to meet it, and not to cash it until the next day, and the fact that the claimant was anxious for the payment of his debt, and that the claimant was several days in securing his money, were such facts as would put a reasonably diligent man upon inquiry as to the financial condition of the bankrupt. The circumstances in this case surrounding the transactions between the claimant and the bankrupt as to putting the claimant upon notice are far stronger than those in the Dorr case. In the

present case the credit man of the claimant was informed that the company had no money with which to pay its obligation, that its production was not sufficient to meet its small bills; that if the claimant expected anything on account it would be necessary for them to take property belonging to the bankrupt and credit it on account. Furthermore, the claimant was aware of the fact that the stock of the bankrupt had declined until it was worthless, and of no market value, and that the financial condition of the company was precarious. It also was aware that there was other small creditors who were unable to obtain payment from the bankrupt. Under the rulings in the above cases and under the rule of law as laid down by the federal court, that the appellate court will not disturb the findings of fact of the referee and the district court when the same are made on conflicting evidence, this court would hardly be justified in finding that the evidence in this case was insufficient to constitute the payments made preferences.

WHERE THERE IS A CONFLICT OF TESTIMONY, THE APPELLATE COURT WILL NOT REVERSE THE DECISION OF THE LOWER COURT.

In this case there is a substantial conflict of evidence. On one side we have the circumstances surrounding the preferential payments showing that at the time they were made that the claimant was informed that the bankrupt had no money and that the only payment that the bankrupt could make was to return certain casing and pumps which it had on hand, and prior to the time of said payments that the credit of the bankrupt with

the claimant had been entirely cut off and that the claimant had been insisting and demanding its money from the bankrupt, and had threatened to make the surety of said bankrupt pay the same, and that it had refused to deliver any goods in any amount to said bankrupt without immediate cash payment for the same, together with the correspondence of Mr. Sands, the credit man for the claimant, with the various stores of claimant showing that Mr. Sands was acquainted with the financial irresponsibility of the bankrupt. On the other hand we have the testimony of Mr. Sands to the effect that he at all times considered said account a solvent one, and that he did not have the least suspicion that at the time he received said payments that the bankrupt was insolvent or that his firm was receiving a preference. The referee and the district court decided that each of these payments was a preference after hearing and considering all of this testimony; and this being the case, the appellate court should be very reluctant to reverse the decision of the referee and the United States court where the referee had the opportunity to personally observe the witness and to take into consideration their attitude while testifying. In such cases it has been repeatedly held that the appellate court will not disturb findings of fact made by the referee and district court on conflicting evidence. In the case of Boswell National Bank v. Simmons, U. S. Circuit Court of Appeals for the Eighth Circuit, Judge Adams said:

"When the trial court has considered conflicting evidence and made its findings of fact, they must be taken to be presumably correct, and this presumption is ma-

terially strengthened by the master's prior findings to the same effect."

Concluding, after a careful consideration of the proof in this case, that there was substantial evidence to sustain the findings of fact, and discovering no obvious errors of law or serious mistake of law in such findings, the presumption of their correctness must be indulged.

Boswell National Bank v. Simmons, 26 Am. B. R. 865.

In the case of Page v. Rogers, 211 U. S. 575, the Supreme Court had an opportunity to discuss this proposition in a preference case, and used the following language:

"The rule is well established that where two courts have concurred in the findings of fact in a suit in equity, this court will accept these findings unless clear error is shown."

In Cenner v. Webster-Tapper Co., 168 Fed. 519, Judge Loland, in discussing a preference case, cited the case of Page v. Rogers, and said:

"We conceive no error in the findings of fact made by the referee and confirmed by the judge. These we are to accept, unless error in them is shown."

In re Dorr, 196 Fed. 292, the rule in a preference case was laid down as follows:

"Where the testimony is conflicting and the findings of fact of the referee and district judge are the same, the facts will not be inquired into by an appellate court unless there is plain error."

In De Laval Separator Co. v. Iowa Dairy Separator Co., 194 Fed. 423, Judge Sanborn, speaking for the court, said:

"When the chancellor has considered conflicting evidence and made his findings and decree thereon, they must be taken to be presumably right, and unless an obvious error has intervened in the application of the law or some serious mistake has been made in the consideration of the evidence, they must be permitted to stand."

In the case of Vanderbilt v. Bishop, 199 Fed. 420, Judge Ross, speaking for the court, said:

"In the circumstances appearing, the general rule applicable to such cases precludes us from interfering with the findings of the trial court, having the advantages alluded to."

In conclusion, we wish to call attention of the court to the opinion of the learned referee, in which both the law and the facts of this case are discussed at length with unusual clearness and perspicuity. [Tr. pp. 9 to 23, inclusive.]

It is respectfully submitted that the judgment of the United States District Court should be affirmed.

HICKCOX & CRENSHAW,

Attorneys for William H. Moore, Jr., Trustee in Bankruptcy of the Cleveland Oil Company, Bankrupt, Appellee.

No. 2254

In the United States Circuit Court of Appeals

For the Ninth Circuit

R. H. HERRON COMPANY, a corporation,

Appellant,

vs.

WILLIAM H. MOORE JR., Trustee in Bankruptcy of the Cleveland Oil Company, a corporation,

Appellee.

REPLY BRIEF OF THE R. H. HERRON COMPANY, CLAIMANT AND APPELLANT.

RESPONDENT HAS FAILED TO SHOW THAT THE PAYMENTS CONSTITUTED PREFERENCES.

Counsel in their reply brief first assert that the findings of the Referee to the effect that at the time the payments were made was insolvent was sufficiently supported by the evidence. After a review of the testimony they say (page 7) "It can hardly "be contended that these assets out of which the

"trustee did not realize in excess of $10,000.00 "were at any time during the four months of suf- "ficient value to pay the unsecured indebtedness of "the company amounting to over $57,000.00."

It may be remarked here that the unsecured debts did not amount to $57,000.00 and over, but according to the schedule in insolvency were $34,-234.61 (Supp. Tr. p. 18). This is the amount stated by the Referee as the unsecured indebtedness (Tr. p. 10). In fact counsel in their brief place it at this sum (p. 6 Respondent's Brief).

To support this conclusion they say that the property which came into the hands of the trustee being property held by the bankrupt at the time of the filing of the petition did not exceed the sum of $10,000.00; that both France and Batchelder testify there was no change in the assets of the company at the time of the bankruptcy; that the leases were of very doubtful value and were forfeited to the lessors.

In reply appellant contends that counsel for the respondent are drawing their conclusion from the facts that appeared at the time of the insolvency some months later and not by those that are in evidence as of the dates of the transactions attacked. At the time of the alleged preferences the insolvent company had valuable leases. These are ignored entirely by counsel or are dismissed with the statement that they were of very doubtful value. It is not denied by respondent that at the time of the alleged preferences the insolvent was in possession of and the owner of these leases. That they were

not of very doubtful value is shown by the testimony of witnesses called by the trustee himself.

Mushet, our expert accountant, who made an examination of the books and made a report after the date of the alleged preferences, reported as among the assets "oil properties and leases $253,163.05" and "development work in different companies $172,852.35" (Tr. p. 57).

This would certainly indicate that the leases were not valueless or of very doubtful value at the time of the payments. The fact that they were afterwards forfeited and became of no value as assets to the bankrupt is not a proper subject for consideration here.

Furthermore, Sands testified that at "this particular time this company had a lease on what was "and is considered a very valuable piece of oil territory, as I understand it in the Midway field" (Tr. p .72).

He further said (p. 94) "It was adjoining the "Buick Oil Company property, which is one of the "best properties, we understand, in the state; it "joined that."

It also appears that on December 20, 1910, the New York Midway Oil Company was trying to arrange to take over the property. The secretary of this company at that date wrote, among other things, as follows (Tr. p. 146):

"It is the intention of the New York Midway Oil "Company to settle with all these creditors, to ad-"just all matters now in litigation and to save to "the individuals who are stockholders of the Cleve-

"land Oil Company the equity they now have in "the property."

This is significant in view of the claim that the leases were of very doubtful value. It is hardly to be supposed that the new company would settle with all the creditors, would adjust all the matters in litigation and save the equities to the stockholders if the leases were of no value.

The record also shows that the trustee contested the forfeiture of one of the leases very vigorously (Tr. p. 52). Certainly this would indicate that the trustee regarded the lease as valuable. He would hardly contest the forfeiture vigorously if he considered the lease as valueless.

It also appears that the property covered by this lease was afterwards leased to and was being pumped and operated by the Midway Field Company (Tr. p. 52). This too shows the lease was valuable for it is not customary for an oil company to lease, pump and operate property unless it is valuable, unless it pays them to do so. Especially is this so where a company leased property after it has been leased to and operated by another company, For if the operation of the property by the first company had shown it to be without value no other company would ever lease it.

The fact that afterwards the leases were forfeited and went back to the owners and therefore did not add to the distributable assets of the Cleveland Oil Company is not a proper matter of consideration in determining the rights of the plaintiff. One of the leases the trustee let go by default; another he

lost on a contest (Tr. p. 52). These are facts occurring afterwards and therefore have no weight. The controlling fact is that at the times of these payments the Cleveland Oil Company was in possession of these leases. They were of value. This is shown by the report of the expert Mushet. It is shown by the attempt of the New York Midway Oil Company to take over the property, pay all the debts, protect the stockholders and reorganize the company. It is shown by the fact that some of the property was afterwards leased to and was being pumped and operated by another company. It is shown too by the acts of the trustee himself in vigorously contesting the forfeiture of the lease.

It follows that the claim of counsel for the respondent that the assets during the four months' period were not enough to pay the unsecured indebtedness—$34,234.61—is not supported by the evidence.

If through the precipitancy of creditors and the default or misfortune of the trustee the assets which the company had at the time of the payments were subsequently lost, this does not affect the validity of the payments to the claimant and should not be given the slightest consideration.

Continuing counsel say (p. 8) that "at the time the "payments were made, the bankrupt by the testi- "mony of its officers, Edson France and W.J. Batch- "elder, not only knew that it was insolvent but knew "it was irretrievably so, and that it could not make "the payments that it did without disparity in pay- "ments to its other creditors."

They do not refer to any evidence in the transcript to support this statement. Certainly so sweeping an assertion should be based upon very positive testimony.

The testimony of Batchelder is on pages 115-119 of the transcript. An examination of it does not show in any particular that he knew the company was irretrievably insolvent. There is not a syllable of his testimony to show that he had any knowledge of the financial condition of the company at all. On the contrary he says that he did not handle the accounts, but that the treasurer, Edson France, had charge of the accounts and conducted most of the negotiations (Tr. p. 118).

Edson France directly testified that at this time he did not consider the company in very bad shape financially (Tr. p. 38).

As counsel rely upon these two witnesses to support this statement, the foregoing references show that the assertion made by them is without any support whatever.

Counsel say that the trustee was at a great disadvantage in this case for the reason that the parties were very reluctant and unwilling to give the court the information which they possessed; that because of this the trustee was unable to present to the court a full and complete statement of the transactions between the claimant and the bankrupt.

They say that Mr. Sands was a reluctant and an unwilling witness as he was one of the officers of the claimant and very desirous that his company's claim should be allowed. They say further that Mr.

France and Mr. Batchelder were reluctant and unwilling witnesses as they were under arrest by the United States postal authorities on account of transactions connected with the Cleveland Oil Company.

Mr. Sands, Mr. France and Mr. Batchelder were all witnesses called by the trustee. They were his witnesses and not the plaintiff's. This counsel are attacking the fairness, integrity and character of their own witnesses.

If the insinuations of counsel are based on the truth, they being trustee's witnesses and the ones upon whose testimony the trustee relies to establish the alleged prefences, it may be asserted that the trustee has failed to sustain the burden of proof cast upon him. If his witnesses are unworthy of belief, he can hardly expect to prove his case by them. As to the statement that Mr. France and Mr. Batchelder were under arrest by the United States postal authorities on account of transactions connected with the Cleveland Oil Company, there is nothing in the record to support it. This fact nowhere appears in the transcript. Thus counsel have gone entirely outside of the record to attack their own witnesses.

But suppose counsel's charges and insinuations were true—which is not admitted by appellant—that does not justify the statement that the trustee was at a great disadvantage in this case. If, as he claims, the company was so irretrievably bankrupt at the time and its affairs were such that an inquiry would have put the plaintiff on notice, these facts could have been proved by other evidence. He

could have introduced the evidence of other creditors and of bankers and have shown the general reputation of the company in the community. He failed to do so. The burden of proof is on the trustee. If his proof is insufficient, his case falls. But under no circumstances should he be permitted to sustain his case by attacking the credibility and character of his own witnesses.

Counsel next refer to the fact that the plaintiff here was suspicious and had cut off the credit of the Cleveland Oil Company as showing that it had reasonable cause. They say that as early as January 11, 1910, the plaintiff had become suspicious and that on January 21, 1910, the treasurer of the claimant wrote that the credit given the Cleveland Oil Company was quite enough as it was owing considerable sums for other bills and other creditors were not able to get their money.

These events were months before the transactions here attacked. That the claimant here acted in entire good faith is shown by the fact that subsequently it sold to the Cleveland Oil Company thousands of dollars worth of goods. It has been shown in the opening brief that the credit of the company was never entirely cut off; that the company was privileged to call at their stores at Bakersfield, Taft and Maricopa for emergency supplies and that for anything in excess it was to communicate with the Los Angeles office (Opening Brief pp. 23 and 24).

There is not a line in the transcript to show that the credit was curtailed because of a belief in the

company's insolvency. Mr. Sands testifying as to this says (Tr. p. 70):

There was nothing new in curtailing the credit of the oil company. It was in accordance with their customary treatment of the company. As early as May, 1909, its credit was curtailed (Tr. p. 100). There was therefore nothing at all significant in limiting its credit in July, 1910.

"We considered at that time they were owing us "quite a considerable sum and of course like other "creditors they reached the period where they "should either increase or decrease. At that time we "thought we had given them—that they were up "to the limit of their credit."

This is a simple and perfectly natural explanation from the lips of the trustee's own witness.

Under any circumstances mere suspicion, cutting off of credit, being anxious about the payment of bills or being importunate in their collection does not establish reasonable cause. If they did the business transactions of a community would be very insecure. Payments are made to creditors up to the very day of their failures in entire good faith by creditors who are buoyed up by the hope that they may be able to proceed in business. If mere suspicion were enough to upset a transaction, then few if any acts could stand because any transaction in any degree out of the ordinary is liable to cause suspicion.

That the contention of appellant in this regard is abundantly supported by the authorities is shown by the citations in the opening brief. Attention

is again called to them and particularly to the leading case of Grant National Bank, 97 U. S. 80, quoted at length on pages 17 to 20 of the opening brief. The clear reasoning of this great case applies directly here and fully shows the fallacy of the position taken by counsel.

Counsel next refers to two letters, one written to Mr. Sands on August 22, 1910, the other written by Mr. Sands on October 18, 1910. The first letter discloses nothing suspicious or out of the ordinary but on it Mr. Sands indorsed the following notation: "Keep after them at least twice a day. Make "them come through."

This notation is referred to by the referee and counsel also say that Mr. Sands must have had reasonable cause or otherwise he would not have made such a notation. They further say that they are of opinion Mr. Sands was acquainted with the true condition of affairs because of the letter of October 18, 1910.

It is respectfully submitted that a careful consideration of these letters and of the actions of Mr. Sands taken in connection with them shows that the conclusions of counsel are not justified.

There being some question as to the meaning of Mr. Sands in making the above notation, his actions in reference thereto will throw a strong light upon it. It is well settled that in case of writings that are uncertain, the practical construction placed upon them by the parties themselves and their actions under them are the surest means of ascertaining what was meant. Applying this rule here

and it becomes evident that Mr. Sands meant nothing by the annotation and that he had no suspicion that a preference was intended.

It appears he never went after them twice a day or once a day or at all except in the manner he had always acted. The notation was a mere memorandum addressed to himself. He never communicated it to any, never instructed any one to go after the Cleveland Oil Company. While he wrote to his agents afterwards he never told them to go after the company and never expressed any doubt as to getting the money due his company. Furthermore the notation says "Make them come through." This is as much as to say that the company could come through, had ability to do so if payment was urged. There is no suggestion that it was necessary to go after the company for fear that there was not enough for all the creditors and that the plaintiff might be overreached by the other creditors if it did not keep after the debtor.

The same general conclusions may be reached as to the other letter. In this Mr. Sands says: "The "Cleveland Oil Company owes us considerable "money and they are not in a position to supply "the ready cash. Their stock is almost worthless "from a stock market point of view, the last sales "being passed at 2¾c. They are endeavoring to "arrange the company on a sound financial basis "but that will take some time." (Supp. Tr. p. 37).

Here is not a suspicion of insolvency, not a suggestion that the company will not be able to arrange its affairs on a sound financial basis. The statement

"that will take some time," is equivalent to saying it will be accomplished and can be done, only it will take time. For this reason—that it would take time—and not because the plaintiff suspected insolvency or had reasonable cause to believe a preference was intended, the letter was written by Mr. Sands to his manager informing him why he would accept the pipe and credit the debtor with it. He was explaining to his manager why he was taking the pipe and was directing the manager what to do with it. There is not the slightest intimation in the letter that there was any thought of the insolvency of the debtor, that there was any idea that other creditors were being taken advantage of or that any preference was intended.

This it is respectfully submitted is the only proper construction to be placed upon this letter. These letters have been considered at some length in the opening brief on pages 31 to 34. It is unnecessary to repeat what is there said. But appellant herein respectfully urges that its construction of these letters is correct and that its conclusions are fortified by the practical interpretation placed upon them by the parties themselves.

Counsel next refer to the return of the pipe. They have not however given all of the testimony concerning this particular transaction. It seems that the return of the property was due to a voluntary suggestion on the part of France (Tr. p. 39). France stated to Sands that his company had a string of pipe in the field it was not using (Tr. p. 44). This was the pipe that was returned. It was quite cus-

tomary to take back second hand material (Tr. p. 85). The price at which it was taken was more than a fair price (Tr. p. 85). France told Sands that he had no use for the material and would be very glad if it could be received on account as a credit. (Tr. p. 86).

The complete transaction shows that it was entirely free from suspicion and in absolute good faith with no thought of the insolvency of the debtor or idea of getting ahead of the other creditors. A full account of it is given in the opening brief pp. 27 and 28, and it is respectfully contended that when all the facts are considered, it is not open to attack as a preference.

Counsel next refer to the payment of the $2000.00 but make no argument upon it. This matter is fully explained in the opening brief pages 28 and 29 and what is said there is practically uncontradicted.

Counsel then urge that the claimant's contention that on the 31st day of December, when the pumps were returned it did not have knowledge is wholly without merit.

In this connection they say that the claimant had among its files in its credit department certain clippings from Los Angeles newspapers which recited the fact that the Cleveland Oil Company was in a bad way financially and that its officers were under arrest by the United States postal authorities on account of fraudulent transactions connected with the company.

Concerning this, it may be said that Mr. Sands

said he never read the articles in the newspapers (Tr. pp. 65, 66) and Mr. Sands, it is to be remembered, was a witness for the plaintiff and was testifying on direct examination in giving this testimony. He furthermore says that he had no knowledge as to the clippings; that he did not take the papers from which they were cut and that the clippings must have been cut out by some one who took the paper (Tr. pp. 62, 63). Thus the testimony of the plaintiff's own witness on direct examination disposes of his contention in this regard.

Counsel then urge the rule that notice of any facts that would incite a man of ordinary prudence to inquiry under similar circumstances is proof of all the facts which a reasonably diligent inquiry would disclose.

This rule as an abstract proposition is one which no one will deny. Appellant, however, contends that it has no application here. The facts introduced in evidence here, even if the instruction most favorable to the trustee is placed upon them create nothing more than mere suspicion. It has been abundantly shown in the opening brief that mere suspicion, the curtailing of credit and other steps taken by a creditor to protect itself do not constitute reasonable cause. If they did then no transaction within four months of bankruptcy proceedings would ever stand.

Again even if the appellant here were put upon notice—which is strenuously denied on the showing made in the opening brief—there is nothing in this record to show that he would have learned any-

thing by inquiring. The case here is made up entirely of the dealings between the parties to the transactions here attacked. There is no evidence whatever as to the dealings of the Cleveland Oil Company with third persons as to its general reputation in the community, the number of its other creditors, as to its standing with banks and as to the other various matters which go to show the standing of a business house in a community. There is no evidence to show any of these matters. The trustee has shown nothing which would be developed were an inquiry made. One of the limitations of the rule of notice relied upon is that upon inquiry being made the information would have been obtained. There is nothing in this record to show that upon inquiry any information would have been obtained. The trustee here has contented himself with merely showing the relations between the plaintiff and bankrupt. Had the outside relations of the Cleveland Oil Company been shown there might have been something upon which the rule could operate but not having shown anything, it is pure abstraction as far as this case is concerned. This point has been fully argued in the opening brief on pages 63 to 66 and it is respectfully urged that respondent has not met the contentions there made. Appellant then stated that there was nothing in the record to show that an inquiry would have developed anything or in any way charged the appellant with knowledge. Counsel in reply merely refer to the dealings between the plaintiff here and the Cleveland Oil Company. It

is therefore submitted that the contention of appellant that the rule of notice does not apply here as there is nothing in the record upon which it could operate is admitted.

The authorities cited by counsel are not in point.

In in re Dorr, 196 Fed. 292, the facts in the record were such that an inquiry by the creditor would have disclosed the information as to the condition of the insolvent (See page 296).

The same is true in the other case cited by counsel on this point, the case of in re Deutschle, 182 Fed. 435. In this case the facts which would have been elicited are abundant. The court does, however, in the course of the opinion use language that applies strongly here. In speaking of the effect of not paying notes and frequently allowing them to go to protest as giving a creditor notice, Archibald, D. J. said (p. 437):

"This is not enough. It shows a lack of ready "money, no doubt, and possible embarrassment "but not necessarily insolvency, and was not, there- "fore, of itself sufficient to put the claimant on in- "quiry."

As has been pointed out, the only thing in this whole record to charge the plaintiff was that the Cleveland Oil Company was short of ready cash. It had valuable assets in its leases but it had difficulty in raising the ready money. This is the case of thousands who carry their ventures to successful conclusions. The relations between the parties had not materially changed from the beginning. As early as May, 1909, the credit of the oil company

had been curtailed (Tr. p. 100). Yet after that the plaintiff had sold it thousands of dollars worth of goods without any thought or suspicion of its insolvency. France, the president of the company, was hopeful to the end and believed the company would succeed. Towards the end, a reorganization plan was under way which would probably have straightened out everything and in all likelihood it would have succeeded but for the bankruptcy proceedings.

It is respectfully urged that counsel have failed to show anything justifying the application of the doctrine of notice and that therefore they are not at liberty to invoke it in this case.

THE RULE THAT "WHERE THERE IS A CON-"FLICT OF TESTIMONY, THE APPELLATE "COURT WILL NOT REVERSE THE DECISION "OF THE LOWER COURT" DOES NOT APPLY HERE.

The learned counsel attempt to invoke the rule that where there is a conflict of testimony the Appellate Court will not reverse the decision of the lower court. This is an old rule of procedure and one that has been enunciated by most if not all appellate tribunals. It is, however, a discretionary rule, it always yields when the proper administration of justice demands it and it is as frequently departed from as observed. In reply to the contention of counsel, it is sufficient to refer to the numerous authorities cited and quoted in the opening brief where the Appellate Courts have gone into the evidence and reviewed it for the purpose of determining

whether the facts in the particular case before it constituted a preference. These authorities abundantly show that the rule contended for is far from being an absolute one and that it is never applied where the rights of the parties require an examination into the record.

Were, however, the rule as absolute as the learned counsel would have it, it would not apply here. The rule is invoked where the witnesses on one side contradict the witnesses on the other side of a case. In this case the witnesses were all on one side. The claimant here called no witnesses. The only witnesses called were those called by the trustee. Therefor the respondent stands in the anomaluos position of trying to apply this rule because of the conflicting statements of his own witnesses. The only conflict counsel points out is the alleged contradictory statements of Sands himself. Sands was the respondent's witness. Now counsel urges this court not to consider the appeal on the ground that their own witnesses contradict one another.

It is submitted that so unusual and remarkable a position cannot be maintained. On the contrary, if there is such a conflict of testimony among the witnesses for the trustee, it clearly shows that the respondent here has not sustained the burden of proof which the law imposes upon it.

CONCLUSION.

Appellant in its briefs has gone fully into the evidence as well as the law, feeling that an injustice has been done to it. A careful examination of the record, of the acts of the appellant and of the letters

written by the agents fails to show the appellant had any reasonable cause to believe a preference was intended. There is nothing to show that the appellant had at any time any suspicion of the insolvency of the Cleveland Oil Company. There is nothing to show that at any time it was attempting to overreach any of the other creditors. All of its acts at all times were in the utmost good faith, open and above board and free from all doubt. It is very questionable if the oil company was insolvent at the time of the alleged preferences. It had at that time valuable leases. Afterwards when the creditors precipitated the bankruptcy proceedings and the leases were lost or forfeited, the assets of course were dissipated. But the rights of the appellant here are to be determined by what existed at the time of the alleged preferences. At that time, the company apparently was solvent. One of the reasons for the adverse view taken of the appellant's case has arisen out of confusing the facts existing at the time of the bankruptcy with those that existed at the time of the payments. If only the facts that are in evidence as of the date of the payments are considered and all others are eliminated, it is respectfully submitted that the case will become clear and it will fully appear that there was no reasonable cause to believe a preference was intended.

For the foregoing reasons it is respectfully submitted that the judgment of the United States District Court be reversed,

Respectfully submitted,

GEO. E. WHITAKER,

Attorney for Appellant.